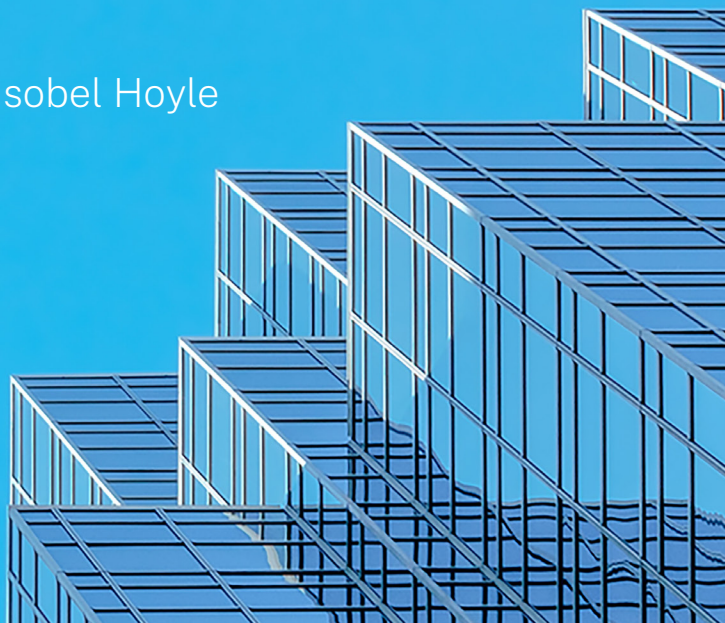

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Global Practice Guides

Corporate Governance

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2025

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INTRODUCTION

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Herbert Smith Freehills Kramer (HSF Kramer) was formed in June 2025 through the transformational combination of Herbert Smith Freehills and Kramer Levin, creating a world-leading global law firm. With over 6,000 people including c.2,700 lawyers and spanning 26 offices, HSF Kramer provides comprehensive legal services across every major region of the world. Uniquely positioned to help clients achieve ambitious objectives, HSF Kramer delivers exceptional results in complex transactions and

high-stakes disputes. The dedicated corporate governance advisory team comprises governance specialists with technical expertise who provide practical advice to clients on the full spectrum of governance issues. The team advises listed and privately held companies on the regulatory, reporting and governance standards applicable to them. The firm draws on its wide-ranging experience to advise on legal and regulatory requirements, emerging trends and market best practice

Contributing Editors



James Palmer is a senior corporate and governance lawyer who was the chair and senior partner of legacy firm Herbert Smith Freehills. He is one of the UK's leading M&A, capital markets and corporate lawyers, with deep experience of corporate governance and regulation, including financial regulation. He is frequently involved in helping clients in situations where they face significant and unusual challenges. These include hostile takeovers, board and governance disputes, regulatory and other investigations, business crises, interactions with governments or government bodies, significant liability or solvency exposures, as well as significant transactions. He is also recognised as a leading expert in relation to both Brexit and foreign direct investment regulation.



Gareth Sykes leads the Herbert Smith Freehills Kramer corporate governance advisory team, advising a range of listed and privately held companies on a variety of governance issues.

Gareth's expertise includes advising on corporate reporting requirements, the UK Corporate Governance Code, continuing obligations pursuant to the UK listing regime, company meetings and directors' duties. A key part of his role is horizon scanning, analysing new laws and regulations to ensure that the firm's clients anticipate and remain at the forefront of corporate governance developments and practice. Gareth writes widely on corporate governance matters.



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Governance in 2025 – Time for a Radical Rethink?

As we set out in our introduction to this Guide last year, 2024 was the year of the election. According to Time Magazine, almost two billion people headed to the polls in 2024, with elections held in over 60 countries (and the EU). By the end of 2024, many incumbent governments had been replaced and many of those which remained in power did so with significantly reduced majorities. The political upheaval of 2024 was therefore a continuation of the volatility we have seen so far this decade arising from the COVID-19 global pandemic, multiple conflicts and global energy crisis. Now that the dust has settled after the elections and the new administrations have taken up office, it seems an appropriate time to consider whether this volatility, and its impact in the world of governance, will continue into 2025.

It is obviously still early days but there are signs that a number of administrations are, at varying speeds and to varying degrees, taking the opportunity to shake up the system. Some are engaged in discussions about how to reshape radically the regulatory landscape in a bid to drive growth, increase productivity and harness the possibilities offered by emerging technology. To respond to this, companies need good lead-

ership and robust governance structures and procedures.

Reducing Regulation to Boost Growth

The COVID-19 pandemic and the measures introduced to try and contain its transmission, had a profound impact on the global economy. Entire industries were shut down or had to adopt new practices, resulting in significant sectors of the global workforce that were unable to perform their jobs in the usual way, or even at all. Supply chains were thrown into chaos as transport routes were disrupted and consumer habits changed overnight. And governments deployed huge sums of money in efforts to protect their citizens' economic livelihoods and health (through containment and immunisation initiatives).

In the aftermath of the pandemic, governments are now facing the dual challenge of regenerating their economies, and servicing the debt accumulated in their COVID-19 response. In a bid to boost growth, governments are exploring how regulation, in governance and other aspects, may be adding to the cost of running businesses and stifling innovation. In the UK for example, the new Labour government is working with regulators to identify areas where regulation can support its growth mission, both through

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removing obstacles to business efficiency and utilising innovation to drive it. Regulators which have been tasked with reviewing their current rulebooks include the Financial Services Authority and the Competition and Markets Authority.

In an EU context, Mario Draghi, the former European Central Bank chief, published a report on the future of European competitiveness in September 2024. The report, which will inform the EU Commission's political guidelines for 2024 to 2029, looks at how to boost sustainable growth, identifies key barriers preventing Europe from reaching its full potential and presents a new industrial strategy for the EU.

Looking to the US, there has been much attention on initiatives being introduced by the US government to reduce the level of regulation and perceived bureaucracy, in a bid to drive US economic growth and prosperity. An early example of these initiatives is the decision of the US Securities and Exchange Commission (SEC) to cease its defence of the rules that it had proposed in relation to climate-related disclosures by listed entities. Having been adopted by the SEC in 2024, the rules had been challenged by various interested parties on account of the anticipated burden they would place on in-scope companies and the potential for conflict between the US rules and climate-related disclosure requirements in other jurisdictions, and were subject to judicial review. The decision of the SEC to cease its defence means that these disclosure obligations are unlikely to survive under the current US government, although California and other US states have continued to regulate climate reporting at the state level. More broadly, the newly established Department of Government Efficiency has been tasked with looking at federal spending and making recommendations for reform.

While companies will no doubt welcome a reduction in their regulatory burden, boards may at times also consider whether any of the measures being revised remain beneficial in the context of their companies' specific strategies and culture. The views and interests of key stakeholders in the company will be fundamental in this assessment.

Reducing the Reporting Burden

Corporate reporting is an aspect of the governance landscape which many jurisdictions are currently evaluating, to ascertain whether the correct balance is being attained. On the one hand, there are the benefits of transparency for shareholders and other interested stakeholders (including regulators and wider market participants) but against that the costs of monitoring, gathering and disseminating this information need to be factored into the equation. Candid consideration of costs of transparency has not been a primary consideration in expanded governance transparency for some years. A well-balanced system will aim to deliver decision-useful information to the relevant stakeholders, without imposing disproportionate costs or stifling entrepreneurialism. It will also need to be kept under regular review to ensure that a reasonable balance is maintained.

Narrative, non-financial disclosures have in recent years added significantly to the volume and complexity of the reporting obligations placed on companies, particularly in the area of environmental, social and governance (ESG) reporting. There are initiatives in place in a number of jurisdictions to re-evaluate these obligations and assess whether an appropriate balance is currently being achieved.

In the UK, the government is continuing with the review of non-financial reporting requirements,

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which was launched by the previous government towards the end of its term in office. A number of changes have already been introduced which are aimed at, or will have the effect of, reducing the disclosures expected by companies. For example, companies are only subject to certain reporting requirements if they meet prescribed size thresholds, with the effect that the greatest level of disclosure is expected from the companies with the largest employee headcount, turnover and balance sheet totals. From April 2025, the monetary thresholds used for the classification of companies have been increased by approximately 50%, which according to the government will result in up to 132,000 companies moving to a smaller size category. This is substantially larger than the increase which was introduced to the equivalent EU monetary thresholds in 2024. Certain disclosures viewed as being unnecessary or duplicative are also being removed from the directors' report and the directors' remuneration report which make up part of the annual report and accounts companies need to produce each year under the UK reporting regime.

It seems to us there is significant scope for further lightening of reporting burdens – the momentum to the removal of regulatory burden in financial services regulation is materially further progressed than that for wider corporate reporting – if UK Prime Minister Keir Starmer's commitment to removing 25% of the cost of regulation for businesses is to be achieved in the near future.

In Australia, the adoption of the Fifth Edition of the ASX Corporate Governance Principles and Recommendations, which was expected to apply to listed entities in place of the Fourth Edition for financial years commencing on or after 1 July 2025, was cancelled in February

this year. The updated edition would have introduced significant changes, including to embrace the importance of a company's relationship with its shareholders and of board and workforce diversity. Aspects of the draft Fifth Edition were negatively received by certain parts of the governance ecosphere, and ultimately the ASX Corporate Governance Council, the independent body charged with drafting the updated edition, was unable to agree a final text. The Fourth Edition, published in 2019, therefore remains in place as the standard to be applied.

The amendments made to the EU monetary thresholds in 2024 lifted a number of companies out of the scope of the Corporate Sustainability Reporting Directive (CSRD), as well as other EU reporting requirements. However, the EU Commission is proposing amendments to the size thresholds in the Omnibus Package which would have a greater impact on the applicability of the CSRD and the EU Taxonomy for sustainable activities. Amongst the Omnibus proposals are measures which would significantly increase the size threshold based on employee numbers for determining applicability of these legislative instruments and would require that the employee number threshold should always be met (under the current approach any two out of the three threshold criteria need to be met to bring an entity in scope). As well as amendments to the thresholds for applicability, the Omnibus package also contains measures to simplify the EU's sustainability framework (which is highly technical and which many organisations have struggled to implement) and measures have already been passed to postpone the reporting requirements contained in the CSRD and Corporate Sustainability Due Diligence Directive (CS3D) for certain companies. Whilst the measures are broadly welcomed, proposing changes so soon after the framework has been

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adopted and, in the case of the CSRD, during its phased implementation, has caused uncertainty for companies, many of which have already dedicated significant resources in responding to these directives.

An aspect of reporting which can place additional strain on companies' resources is the fragmentation of reporting frameworks adopted in different jurisdictions. This lack of cohesion is also detrimental to investors and other interested stakeholders as it makes it far harder to compare entities which are subject to different reporting regimes. The International Sustainability Standards Board (ISSB) was created in 2021, with a mandate to develop international sustainability disclosure standards. These standards are designed to operate for sustainability-related reporting in the same way as the IFRS framework operates for accounting standards. The ISSB issued the final form of its first two sustainability disclosure standards (ISSB Standards) in June 2023 and now individual jurisdictions are determining whether, and how, to incorporate these standards into their domestic reporting framework. It is hoped that the ISSB Standards will become as universally endorsed and applied as the IFRS's accounting standards, which would assist entities operating in, and subject to the reporting requirements of, multiple jurisdictions.

Embracing Innovation

Governments can help to boost growth and economic performance by ensuring that businesses can take maximum advantage of technological tools to drive efficiency, and by removing unnecessary barriers to the deployment of these tools. Again, there are examples of governments exploring how to incorporate technological advancements into best corporate governance practices.

An example of such an initiative is the UK government's stated plan to review the law relating to virtual annual general meetings (AGMs). Whilst relaxations were introduced during the COVID-19 pandemic to allow companies to hold their AGMs virtually, these relaxations were subsequently removed once restrictions on travel and gathering in groups were removed. In light of the experience during the pandemic, the UK government has announced that its push to modernise company law will include clarifying the law in relation to the legality of virtual AGMs. This is an approach already permitted in Australia, where companies can hold fully virtual AGMs if the company's constitution permits this. The Australian Securities and Investments Commission (ASIC) maintains guidance for companies which sets out FAQs on fully virtual meetings and hybrid meetings, clarifying that the law does not mandate a particular meeting format. There are various factors a company would need to weigh up when deciding which meeting format is most suitable in its individual circumstances but introducing this flexibility, and removing the current uncertainty, would be a further step in modernising shareholder engagement and communication in the UK.

Whilst corporate governance initiatives may not grab all the headlines, there are steps being taken in many jurisdictions which will have a meaningful impact on how companies are managed and administrated. The summaries presented in this Guide for individual jurisdictions provide a clear overview of the corporate governance framework being applied in those jurisdictions and also highlight some of the hot topics and trends currently being seen. The Guide will therefore be a useful resource for companies as they navigate the regulatory landscape in the jurisdictions in which they operate.

ARMENIA

Law and Practice

Contributed by:

Hayk Hovhannisyan and Suren Sloyan

HAP



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HAP blends professional experience with the energy of younger talent in its provision of a wide range of legal services. It advises on all aspects of corporate governance and combines deep regulatory knowledge with practical insight into clients' business needs. The firm guides companies, boards, shareholders and executives through complex compliance frameworks, shareholder relations and governance

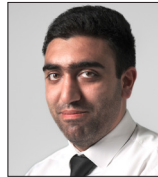
structures, both in day-to-day operations and during critical transitions. It converts its significant academic knowledge into practical representations of institutional investors in complex insolvency proceedings. During its ten years of practice, the firm has earned its place as an experienced legal services provider in corporate, commercial, administrative law, IT, IP, banking and construction industries.

Authors



Hayk Hovhannisyan of HAP has more than 25 years of multi-jurisdictional experience in corporate, transactional and dispute-related matters. He has a particular focus on cross-

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Businesses may operate in various organisational and legal forms in Armenia. The organisational and legal form is chosen taking factors such as the scope of liability, the number of participants and the applicable tax regime into account.

The main forms of corporate and business organisation in Armenia include the following.

Limited Liability Company (LLC)

An LLC is the most common and flexible business structure. Under this structure, shareholders are only liable to the extent of their contributions to the charter capital. There is no minimum charter capital requirement and this form of organisation is suitable for small and medium-sized enterprises (SMEs).

Joint Stock Company (JSC)

JSCs can be open or closed.

Open JSC (OJSC)

In OJSCs, shares are freely transferable and can be publicly traded.

Closed JSC (CJSC)

In CJSCs, shares are distributed among a limited number of shareholders and are not freely traded. They are suitable for large businesses seeking investment.

Co-Operatives

Co-operatives can be formed by individuals with shared economic interests. They are typically used in agriculture, housing and small-scale production.

Individual Entrepreneur (IE)

An IE is a business which is owned and operated by one individual. In an IE, the owner has full control but also unlimited personal liability for debts. There is simplified registration and tax treatment for IEs. This structure is ideal for new businesses because of its straightforward management and operational simplicity.

Contract of Joint Activity Without Forming a Legal Entity

IEs and/or commercial organisations and/or citizens engaged in agricultural production can pool their resources and act jointly without establishing a separate legal entity for the purpose of making a profit or achieving other lawful objectives.

Participants may contribute professional expertise, skills, business reputation and connections as well as capital.

During joint activities, each participant may act on behalf of all, unless otherwise specified in the contract, which may require joint action by all parties.

This form of organisation is particularly effective when an individual has skills or expertise but lacks financial assets.

Each of these business forms should be carefully evaluated to determine the most appropriate legal entity for establishment based on the specific needs and goals of the business.

1.2 Sources of Corporate Governance Requirements

The primary legislative sources of corporate governance requirements for companies in Armenia are as follows.

The Civil Code of Armenia (CC)

The CC defines the concept of a legal entity, its types, legal capacity, liability, redomiciling procedure, reorganisation procedure, liquidation procedure and other general principles.

The Law on Joint Stock Companies (LJSC)

The LJSC regulates the structure, governance and operational processes of JSCs. It outlines the rights of shareholders, the duties of the board of directors (BoD) and the requirements for financial transparency and disclosure. It also sets out provisions for annual meetings, dividend distribution and financial reporting obligations.

The Law on Limited Liability Companies (LLLC)

The LLLC governs the operations of LLCs. It focuses on shareholder rights, management structures and decision-making processes. It provides a framework for the internal governance of LLCs, ensuring clarity in the roles and responsibilities of owners and managers.

The Law on Bankruptcy

The Law on Bankruptcy governs insolvency proceedings and the restructuring of companies. It establishes the rights and obligations of creditors as well as the roles of corporate management during insolvency, ensuring a structured process for debt resolution and corporate recovery.

The Law on State Registration of Legal Entities

The Law on State Registration of Legal Entities establishes requirements for the registration of companies and their ongoing obligations under Armenian law, including compliance with governance standards.

Armenian Securities Market Legislation

Armenian securities market legislation includes regulations on public companies and the governance of stock exchanges, market participants and the protection of shareholders in publicly traded companies.

These legislative sources together shape the corporate governance framework in Armenia, ensuring that companies operate transparently, remain accountable to stakeholders and comply with domestic and international legal standards.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with publicly traded shares in Armenia must adhere to specific corporate governance requirements to ensure transparency, accountability and protection of shareholder interests. These requirements are designed to align with international corporate governance practices and Armenian law.

Corporate Governance Requirements for Publicly Traded Companies in Armenia

Publicly traded companies in Armenia are primarily governed by the LJSC, the Law on the Securities Market and regulations set out by the Central Bank of Armenia (the “CBA”) and the Central Depository of Armenia. These legislative provisions are intended to ensure effective governance, safeguard shareholder rights and maintain market integrity.

Mandatory v Voluntary Requirements

Mandatory requirements

The mandatory requirements are as follows.

- Compliance with the relevant laws and other legal acts.
- Regular disclosure of financial statements and material events to ensure transparency.
- Holding annual general meetings (AGMs) and ensuring minority shareholder rights.
- Establishment of key board committees.
- Conducting external audits and providing transparent financial reporting in line with regulatory standards.

Voluntary requirements

The voluntary requirements are as follows.

- Adherence to the Corporate Governance Code, which provides recommendations for best practices but is not legally required.
- Non-binding recommendations for the composition of the BoD (eg, the percentage of independent directors).

While mandatory requirements ensure legal compliance, shareholder protection and financial transparency, voluntary corporate governance practices, like following the Corporate Governance Code, enhance reputation, investor trust and risk management.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Armenia’s corporate governance landscape is undergoing significant transformation with a pronounced emphasis on sustainability and green initiatives. Key developments include the following.

National Sustainable Finance Roadmap

In October 2023, the CBA introduced the National Sustainable Finance Roadmap (the “Roadmap”), underscoring a strategic commitment to sustainability within the financial sector. The Roadmap is structured around four key pillars:

- mobilising sustainable finance: facilitating capital flow towards industries aligned with Armenia’s low carbon ambitions and introducing innovative financial instruments such as green, blue, social, sustainability and sustainability-linked loans and bonds;
- enhancing markets: establishing a Central Sustainable Finance Database and designing frameworks to monitor progress in sustainable finance initiatives;

- embedding sustainable finance: developing a robust supervisory framework within the CBA, guiding financial market participants in integrating environmental, social, and governance (ESG) factors into their core processes; and
- building awareness and capacity: raising awareness and enhancing knowledge on sustainability risks and opportunities among financial market participants and the wider public.

These pillars collectively aim to ensure that ESG considerations are central to financial decision-making, reflecting Armenia's dedication to sustainable practices.

The Green Agenda Project

The Green Agenda Project was launched in December 2023 and represents Armenia's commitment to aligning with the European Green Deal and the EU-Armenia Comprehensive and Extended Partnership Agreement (the "CEPA"). This initiative seeks to harmonise national policies with leading European standards, propelling Armenia towards a more sustainable and prosperous future. Key objectives of the Project include:

- developing a climate neutrality roadmap.
- delivering investment-ready projects that promote sustainability.
- raising public awareness about the green economy; and
- enhancing stakeholder capacities for the green transition.

The Project underscores Armenia's dedication to adopting sustainable policies and practices and aims to enhance the quality of life for its citizens as well as strengthen trade and economic relations with EU member states.

2.2 ESG Considerations

ESG reporting issues in Armenia are primarily regulated by the Corporate Governance Code, which was updated in July 2024. The Corporate Governance Code emphasises the importance of corporate governance principles for sustainable private sector development, accountability and decision-making transparency. Companies adhering to the Corporate Governance Code have to prepare and publish an annual report.

This has to include a corporate governance report and an annual corporate governance declaration and has to be published on their website by June 30 of the following year. This reporting follows the "comply or explain" principle, which allows organisations to either comply with the Corporate Governance Code's provisions or explain their reasons for non-compliance.

Despite the structured framework, companies face several challenges in ESG reporting. These are as follows.

- Lack of awareness: many stakeholders, including BoD members and executives, may not fully understand their roles and responsibilities within the corporate governance framework, leading to ineffective decision-making and accountability issues.
- Enforcement deficiencies: while legal frameworks exist, the enforcement and monitoring mechanisms are often inadequate. Regulatory bodies may lack the necessary resources and authority, resulting in organisations viewing compliance as a formality rather than a necessity.
- Standardisation and consistency: the absence of standardised ESG reporting frameworks leads to inconsistencies. Companies might adopt different frameworks, mak-

ing it challenging to compare and assess ESG performance accurately.

- Stakeholder engagement: effectively engaging diverse stakeholders, such as investors, customers, employees and regulators, each with unique expectations, poses a significant challenge in ESG reporting.
- Regulatory compliance: keeping abreast of evolving regulations, especially for companies operating in multiple jurisdictions, adds complexity to ESG reporting efforts.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The governance and management of a company are primarily regulated by the CC, the LJSC or the LLC.

The principal bodies involved in corporate governance typically include the following.

General Meeting of Shareholders (for JSCs) or Participants (for LLCs)

The general meeting of shareholders (for JSCs) or participants (for LLCs) is the supreme governing body of the company. It makes key decisions such as approving financial statements, distributing profits, appointing/removing directors and amending the company charter.

The BoD

The BoD carries out the general management of the company's activities, except for those matters that are reserved for the competence of the meeting by the law and the company's charter.

Executive Body (Director or Management Board)

The executive body (director or management board) is responsible for daily operations. It can consist of a sole director (CEO) or a collective management board. It implements the decisions of the general meeting and/or the BoD.

3.2 Decisions Made by Particular Bodies

Specific corporate bodies in Armenia have defined decision-making powers and specific decisions are reserved exclusively for particular bodies.

Typical decisions made by each corporate body are as follows.

General Meeting of Shareholders (JSC)/ Participants (LLC)

The general meeting of shareholders is the supreme governing body and is responsible for key strategic and ownership-related decisions. It makes exclusive decisions which cannot be delegated to other bodies. It can amend the charter (including changing the company name, registered capital, business activities). It is also responsible for reorganising or liquidating the company, approving annual financial statements and profit distribution and deciding on increases or decreases of charter capital.

Additionally, it is responsible for appointing or removing BoD members (if applicable) and appointing/dismissing the executive director if there is no BoD. It can also approve major transactions exceeding a certain threshold and take merger, acquisition and restructuring decisions.

The BoD

The BoD can:

- determine the main directions of the company's activities;
- convene annual and extraordinary shareholders' meetings;
- approve the agenda of meetings;
- approve the year, month, date for compiling the list of shareholders entitled to participate in the meetings and resolve all issues related to the preparation and convening of meetings and reserved for the BoD's jurisdiction;
- approve the administrative and organisational structure of the company;
- approve the annual budget and the implementation of the annual budget;
- approve the company's staff list;
- establish branches and representative offices, which will be institutions of the company; and
- other powers granted by law.

Executive Body (CEO/Management Board)

The executive body (CEO/management board) is responsible for the daily operational management and execution of the company's strategy, signing contracts and managing business operations and managing employees and implementing policies. It is also responsible for:

- handling financial transactions within limits set by the BoD or general meeting;
- representing the company before third parties, courts and regulators; and
- other powers granted by law.

3.3 Decision-Making Processes

General Meeting of Shareholders/Participants

The general meeting of shareholders is the supreme governing body and makes major decisions. It will have quorum if it is attended by participants who hold more than half of the votes of the total number of members of the company.

It will take decisions by a vote of the total number of participants in the company by majority unless the law or the articles of association of the company provide for a greater number of votes to make the decision.

Amendments to the articles of association and authorised capital require at least a two-thirds majority unless stated otherwise. Reorganisation and liquidation decisions must be unanimous. Decisions of the general meeting of shareholders are adopted by open voting, unless otherwise stipulated by the company's charter.

BoD

The BoD is responsible for overseeing the company's corporate strategy and supervising executive management. The decision-making process of the board is typically governed by the company's charter and internal board regulations. Meetings of the board may be held on a regular basis or convened as extraordinary sessions, depending on the needs of the company and procedural rules.

For the board to make valid decisions, a quorum is generally required. This usually means that more than 50% of the BoD members must be present. Decisions are adopted by a majority vote of the members present, unless the company's charter prescribes a higher voting threshold. In cases where votes are equally divided, the chairperson of the board may hold a casting vote.

All board resolutions must be properly documented in the minutes of the meeting and signed by all attending board members. The board may delegate certain decision-making powers to specialised committees or to executive management, depending on the nature of the matter and

the delegation provisions set out in the charter or board policies.

Executive Body (Director or Management Board)

The executive body (director or management board) is responsible for the company's day-to-day operations and for implementing strategic decisions adopted by the shareholders or BoD. The scope of the executive body's authority is defined in the company's charter and in the employment contract of the CEO or general director. Within this framework, the CEO or general director may act independently on behalf of the company, provided they stay within the limits of their authority. Where a collegial management board is established, decisions may be made collectively in line with internal regulations.

The executive body is accountable to the BoD (if one exists) or directly to the shareholders. It has to report on the company's performance and major actions taken. Executives authorised under the charter or by resolution may enter into binding agreements and represent the company in legal and business matters.

4. Directors and Officers

4.1 Board Structure

The structure and functioning of a BoD in Armenia is governed by the LJSC and the LLLC, among other regulations. The structure of a BoD varies depending on the type and size of the company.

A BoD is a supervisory body responsible for overseeing management and board members are elected by shareholders at the general meeting.

In JSCs, the establishment of a BoD is mandatory if the number of shareholders exceeds 50.

BoD members may or may not be company employees. However, executive management (eg, the CEO) cannot simultaneously be the board chair.

4.2 Roles of Board Members

As in most corporate governance systems, a BoD consists of various members with distinct roles and responsibilities. The following is an overview of the key positions and their functions.

Chairperson of the Board

The chairperson of the board leads the board and ensures effective governance. They set the board meeting agenda and preside over meetings. They also act as a liaison between the board and executive management and represent the company in high-level matters. Additionally, they ensure the board follows corporate governance principles.

Board Members (Directors)

Board members (directors) participate in strategic decision-making and oversee the company's financial and operational performance. They ensure compliance with laws and ethical standards and may be executive (involved in daily management) or non-executive (independent oversight).

Independent Directors

Independent directors are not affiliated with the company's management or major shareholders and so can provide objective and unbiased opinions. They enhance transparency and protect minority shareholders' rights. Additionally, they often serve on audit or risk committees.

Executive Directors

Executive directors are typically members of senior management (eg, CEO, CFO) and contribute insights on daily operations. They also implement the board's strategies and policies.

Non-Executive Directors (NEDs)

Non-executive directors (NEDs) do not engage in day-to-day operations. They provide strategic guidance and external perspectives and help with risk management and accountability.

4.3 Board Composition Requirements/Recommendations

The composition and structure of a BoD in Armenia is primarily governed by the LJSC, which outlines specific requirements and recommendations to promote effective corporate governance.

Mandatory Board Establishment

The board must be established in a company with 50 or more shareholders. If a board is not established in a company with up to 50 shareholders, its powers are exercised by the general meeting.

Board Composition Requirements

Independence

In OJSCs, at least one-third of the board members must be independent. The LJSC specifies criteria to determine a director's independence to ensure that these members do not have significant ties to the company that could impair their impartiality.

Separation of roles

To prevent conflicts of interest, the roles of the chief executive officer (CEO) and the chair of the board cannot be held by the same individual in OJSCs. This separation ensures a clear distinc-

tion between the management and oversight functions within the company.

4.4 Appointment and Removal of Directors/Officers

The appointment and removal of directors and officers of a company are primarily governed by the LJSC and LLC, along with the company's charter.

Appointment of Directors and Officers

In LLCs, the general meeting of participants appoints the director(s). In JSCs, the BoD (if one exists) or the general shareholders' meeting appoints the executive director or management board.

Types of Directors/Officers

The executive director or CEO is the primary managing officer of the company. The BoD (if applicable) is a corporate governance body that is usually found in JSCs.

Other Officers

These include the chief financial officer (CFO) or other executives, depending on the company's structure.

Appointment Process

The general meeting (or the board, if applicable) votes on the appointment. A contract is signed with the director, outlining duties, remuneration and term of service.

Removal of Directors and Officers

The general meeting of participants/shareholders has the power to dismiss a director.

In some cases, the BoD may also remove the executive director (CEO), depending on the company's charter.

There are certain legal restrictions on who can serve as a director in Armenia.

General Requirements

The director must be a legally competent natural person. Foreign nationals can be appointed unless restricted by specific laws.

Certain industries, such as banks or financial institutions, may have additional regulatory requirements for directors.

Special Rules for Government Officials

Some government officials cannot serve as directors of private companies. This is to prevent conflicts of interest.

4.5 Rules/Requirements Concerning Independence of Directors

The framework governing the independence of directors and the management of potential conflicts of interest in Armenia encompasses various mandatory legal requirements.

Board Composition and Independence

OJSCs are required to ensure that at least one-third of their board members are independent. The law specifies the criteria for determining a director's independence to promote transparency and accountability.

Separation of Leadership Roles

In OJSCs, the roles of the board chair and the CEO cannot be held by the same person. This separation aims to prevent conflicts of interest and promote effective oversight.

Approval of Transactions with Potential Conflicts

Procedures have been revised to enhance transparency in transactions that may involve conflicts of interest. These revisions ensure that the

essential terms of the transactions are clear, decision-makers remain independent and actual or potential conflicts are eliminated.

4.6 Legal Duties of Directors/Officers

The main legal duties of directors and officers of a company are primarily governed by the CC, LJSC, LLC and other related regulations. These duties include the following.

Fiduciary Duties

Directors and officers have a fiduciary responsibility to act in the best interests of the company and its shareholders. This includes:

- acting in good faith and honestly;
- avoiding conflicts of interest; and
- not using corporate opportunities for personal gain.

Duty of Care and Diligence

Directors and officers must exercise reasonable care, skill and diligence while performing their functions. This includes:

- making informed business decisions;
- ensuring compliance with legal and regulatory obligations; and
- overseeing financial management and risk assessment.

Duty to Act Within Powers

Directors and officers must act within the authority given by:

- the company's charter (articles of association);
- the decisions of the general meeting of shareholders; and
- applicable laws and regulations.

Duty to Prevent Insolvency and Mismanagement

If a company is approaching financial difficulties, directors and officers must take reasonable steps to prevent insolvency and must not act in a way that makes the financial situation worse.

Duty to Maintain Corporate Records and Transparency

Directors and officers must ensure that:

- proper accounting and financial records are maintained;
- the company provides accurate financial reports to the relevant authorities; and
- shareholders have access to essential corporate information.

Liability for Breach of Duties

Failure to comply with these duties can lead to:

- personal liability for damages caused to the company;
- civil and administrative penalties; and
- criminal liability in cases of fraud, mismanagement or financial misconduct.

4.7 Responsibility/Accountability of Directors

Directors primarily owe duties to the company itself. They must act in the best interests of the company, ensuring its success and protecting its assets. This typically means acting in the best interests of shareholders.

However, the law also recognises the need for directors to consider the interests of other stakeholders in certain situations. Specifically:

- creditors: when a company is approaching insolvency, directors may have a duty to consider the interests of creditors to prevent

actions that could make the financial position of the company worse;

- employees: while not a primary duty, Armenian employment laws may impose obligations regarding fair treatment and compliance with labour regulations; and
- government and regulatory compliance: directors must ensure that the company complies with tax laws, environmental regulations and other legal requirements.

While the primary duty is to the company and its shareholders, directors must also be mindful of obligations that indirectly benefit other stakeholders, especially in cases involving insolvency or legal compliance.

4.8 Consequences and Enforcement of Breach of Directors' Duties

If a director breaches their duties in Armenia, several parties may have the right to seek a remedy for the breach, depending on the circumstances.

The Company (via Shareholders or the Board)

The company itself, usually through its BoDs or shareholders, can bring a claim against a director for breaching their duties.

In some cases, shareholders may initiate a derivative action on behalf of the company if the board fails to act.

Creditors (in Insolvency Cases)

If the company is insolvent or nearing insolvency, creditors may have a claim if directors acted recklessly, fraudulently or engaged in wrongful trading.

The insolvency administrator (appointed by the court) may also take action to recover damages from directors.

Regulatory Authorities

Regulatory bodies in Armenia, such as the State Revenue Committee or the CBA (for financial institutions), can investigate and penalise directors for breaches related to tax, financial or securities laws.

Consequences of a Breach

If a director is found to have breached their duties, the consequences may include the following.

Civil liability

The director may be required to compensate the company for financial losses caused by their actions. Courts may invalidate transactions made in breach of duty (eg, conflicts of interest or unauthorised deals).

Criminal penalties

If the breach involves fraud, embezzlement or tax evasion, the director could face criminal charges, including fines and imprisonment.

Directors in Armenia are primarily accountable to the company and its shareholders but creditors and regulators can also enforce breaches in certain cases. Penalties range from financial liability to criminal prosecution, depending on the severity of the breach.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In addition to breaches of fiduciary duties and general corporate governance violations, directors and officers in Armenia may face claims or enforcement actions on the following grounds.

Breach of Statutory Duties

Directors are required to comply with Armenian corporate laws, such as the CC and LJSC.

Violations (eg, failure to maintain proper records, mismanagement of shareholder rights) can lead to administrative fines or legal claims.

Fraud and Misrepresentation

Directors can be held personally liable if they engage in fraudulent activities, such as misstating financial statements, hiding company liabilities or engaging in misleading transactions.

Shareholders or regulators (such as the State Revenue Committee) may bring actions in these cases.

Failure to Prevent Insolvency or Wrongful Trading

If the cause of the insolvency (bankruptcy) of the company is the activity (inaction) of the director, who has the right to give binding instructions to the company for execution or the ability to otherwise determine the activities of the company, then in the event of non-fulfilment of the property belonging to the company, additional (subsidiary) liability may be imposed on those shareholders or other persons for the company's obligations.

The actions (inaction) of the director will be considered the cause of the insolvency (bankruptcy) of the company only if they used their rights or abilities as a director to force the company to perform or not perform certain actions, knowing in advance that this would cause the company to find itself in a state of insolvency (bankruptcy).

Tax and Regulatory Violations

Directors are responsible for ensuring the company complies with tax laws, customs regulations and other state obligations.

The State Revenue Committee and other regulators can impose penalties or even criminal

charges for tax evasion, failure to report income or non-compliance with regulatory filings.

Environmental and Consumer Protection Violations

Directors in industries subject to environmental laws or consumer protection regulations can face liability for non-compliance, including fines or operational restrictions.

Can the Liability of a Director or Officer Be Limited in Armenia?

Director liability can be limited but there are important restrictions:

Indemnification by the company

Armenian corporate law allows companies to indemnify directors for legal costs and damages except in cases of fraud, gross negligence or intentional misconduct.

The company's charter or internal regulations may include indemnification clauses.

Directors and officers (D&O) insurance

Companies can purchase D&O insurance to protect directors from personal liability, covering claims from shareholders, creditors or regulators.

However, D&O insurance does not cover criminal acts or deliberate misconduct.

Limitation in corporate by-laws or agreements

Some liability protections can be included in employment contracts or corporate by-laws, such as requiring shareholder approval before a director can be sued in a personal capacity.

However, these clauses cannot override statutory liability (eg, fraud, tax evasion or wrongful trading).

Legal Defences

Directors can defend themselves by proving they acted in good faith, with due diligence and in the best interests of the company.

The business judgment rule could serve as a defence if directors acted in good faith and with reasonable care.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The regulation of remuneration, fees and benefits payable to directors and officers of a company in Armenia are primarily governed by the LJSC, the LLLC, the LC and relevant company charter provisions.

Approvals Required JSCs

BoD or general meeting of shareholders

The general meeting of shareholders generally approves the amount and terms of remuneration for members of the BoD (supervisory board).

If the company has an executive body (CEO, managing director), their remuneration is usually set by the BoD (if such a board exists) or by the general meeting of shareholders, depending on the charter.

Charter requirements

Company charters may contain specific rules or limitations on compensation structures, requiring formal approval from shareholders or the board.

LLCs

General meeting of participants (shareholders)

The general meeting of participants (shareholders) approves the remuneration of the executive body. In single-member LLCs, the sole participant makes these decisions directly.

Restrictions

While there is no general statutory cap on remuneration, it must be:

- consistent with the company's charter; and
- properly approved via internal corporate governance mechanisms.

Conflicts of Interest

Directors must avoid approving their own remuneration without proper corporate approvals.

Transparency

Specific companies (especially listed ones) may have reporting obligations under securities laws or financial disclosure rules.

Tax Compliance

Compensation must comply with tax and social contribution laws, including proper classification (eg, salary v dividend v service fee).

Consequences of Non-Compliance

Invalidity of payments

Payments made without proper approvals may be deemed unauthorised or invalid and the recipient may be required to return the funds.

Liability of directors

Directors or officers who authorise or receive unlawful compensation may be held liable for damages to the company.

Administrative or criminal sanctions

In serious cases, especially where fraud or misappropriation is involved, criminal charges or administrative fines may apply.

Tax penalties

Improper classification or undocumented payments may result in tax audits, penalties and interest for non-payment of taxes or social payments.

4.11 Disclosure of Payments to Directors/Officers

The disclosure of remuneration, fees or benefits payable to directors and officers is primarily governed by the Corporate Governance Code.

Beyond the Corporate Governance Code, Armenian legislation does not compel companies to publicly disclose specific details regarding the remuneration of directors and officers. However, certain sectors such as banking, insurance and investment fund management may have additional disclosure requirements.

Banks for example have to publish financial statements and audit reports, which could encompass information about executive compensation. While general disclosure of director and officer remuneration is therefore not compulsory, companies in specific industries may be subject to more stringent reporting obligations.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The relationship between a company and its shareholders is governed by corporate law, primarily the CC and the LJSC or the LLLC. How

the relationship is structured and the relevant rules and requirements are as follows.

Relationship Between the Company and Shareholders

Ownership and control

Shareholders are the owners of the company. Their ownership is represented by shares (in the case of joint stock companies) or stakes (in the case of LLCs). The extent of their control over the company is typically proportional to the number of shares they own.

Rights of shareholders

Shareholders have various rights, including, but not limited, to the right to:

- vote at general meetings, which influences decisions like electing directors or approving major corporate actions;
- receive dividends;
- access certain corporate information;
- participate in a liquidation process if the company is dissolved; and
- transfer their shares, although there may be restrictions (for example, in LLCs or in closely held companies).

Rules and Requirements Governing the Relationship

Corporate governance

The relationship is primarily governed by the company's charter and the regulations outlined in the CC and the relevant laws. These documents lay out the rules for:

- shareholder meetings: the frequency and procedures for holding shareholder meetings, voting mechanisms and quorum requirements;
- dividends and profit distribution: how and when dividends can be paid to shareholders

and the decision-making process for distributing profits;

- dispute resolution: procedures for resolving shareholder disputes, often involving the court system if disputes cannot be settled internally;
- company's financial transparency: companies are required to maintain accurate financial records and provide certain disclosures to shareholders, typically through annual reports or shareholder meetings; and
- rights protection: Armenian law also protects minority shareholders by requiring certain protections in decision-making processes, ensuring that major decisions do not disproportionately disadvantage them.

Publicly Available Record of Shareholders

Public Registry

The State Register of Legal Entities (maintained by the Ministry of Justice) is the key registry where information about companies is stored and shareholder information is publicly available for LLCs.

The data on the participants of LLCs is public, but in the case of JSCs, there is no public data on the shareholders.

5.2 Role of Shareholders in Company Management

Shareholders have certain rights and powers but their direct involvement in the management of day-to-day operations is generally limited. The degree of shareholder involvement can vary depending on the type of company, the shareholder agreement and the company's governing documents.

The involvement shareholders may have is as follows.

Shareholder Rights

Shareholders have the right to participate in general meetings (either in person or through proxies), where they can vote on significant decisions, such as the election of the BoD, approval of financial statements, amendments to the charter and decisions on dividends.

In specific cases, shareholders may have the right to request additional information or challenge decisions they believe are harmful to the company.

Management and BoD

Companies typically have a BoD that manages the company. The board is responsible for overseeing the company's operations, strategy and major decisions.

Shareholders usually manage the company directly and have the power to elect members of the board and approve key decisions through shareholder meetings.

Majority shareholders (those owning a significant portion of the shares) can have substantial influence over the management.

Minority shareholders have fewer direct powers but are protected by laws that prevent abuse by majority shareholders. They may be able to exercise influence, particularly if there are provisions in the company's articles of association or shareholder agreement allowing minority shareholder rights.

Directing Management

While shareholders do not typically have day-to-day control, they can influence key strategic decisions, such as mergers, acquisitions or significant investments by voting in shareholder meetings.

Shareholders may also propose resolutions that management is required to present at general meetings and they can influence actions through these mechanisms.

Voting on Specific Actions

In specific cases, shareholders can direct management to take or refrain from specific actions through their voting rights. For example, shareholders might approve or block the adoption of a business strategy or major contracts.

Some decisions, such as changes to the charter, liquidation or changes in the legal structure, require shareholder approval.

Shareholders have the power to influence management through voting and shareholder meetings but their ability to directly manage day-to-day operations is limited for the most part. Their power is largely exercised through strategic decisions and oversight of the BoD.

5.3 Shareholder Meetings

Shareholder meetings are mandatory for companies in Armenia. Both LLCs and JSCs have to convene AGMs to ensure proper governance and compliance with legal obligations.

LLCs

Frequency

LLCs must hold an AGM at least once a year. The meeting should be organised within the timeframe specified in the company's charter but no earlier than two months and no later than six months after the end of the financial year.

Notice

Shareholders must receive 20 days' notice before an extraordinary general meeting (EGM) is convened unless the company's charter spec-

ifies otherwise. Notifications can be sent via mail to the shareholder's address.

Agenda

The AGM generally addresses the approval of annual reports, balance sheets, profit and loss statements, profit distribution and decisions regarding annual dividends.

JSCs

Frequency

JSCs have to convene an AGM within six months after the end of the financial year as stipulated in their charter.

Notice

Shareholders must be notified at least 21 days prior to the meeting. Notifications can be delivered through registered letters, personal delivery or electronic methods such as email or application platforms that confirm receipt.

Agenda

Typical items include approval of annual reports, balance sheets, profit and loss statements, distribution of dividends, election of board members, appointment of auditors and decisions on significant transactions.

General Provisions

Convening meetings

The BoD usually convenes general meetings. However, if the board is not formed or fails to act, shareholders owning at least 10% of the voting shares can request a meeting be convened.

Participation rights

Shareholders have the right to attend meetings, participate in discussions, vote on agenda items and exercise other rights defined by law and the company's charter.

Documentation

Shareholders are entitled to access and obtain copies of documents and information pertinent to the agenda items upon request.

These regulations ensure that shareholder meetings are conducted transparently and that shareholders can effectively exercise their rights.

5.4 Shareholder Claims

Shareholders can bring claims against the company or its directors on various legal grounds. These are primarily governed by the CC and the LJSC. Some of the most common grounds for these claims are as follows.

Breach of Fiduciary Duty (Duty of Care and Loyalty)

Directors of the company owe a fiduciary duty to the company and its shareholders. Shareholders can claim that the directors breached these duties by:

- making decisions negligently by failing to act with due care and diligence; and
- making decisions that benefited them personally and were to the detriment of the company.

Violation of Corporate Governance Rules

Directors must adhere to the rules established by the company's articles of association and corporate governance regulations. Shareholders can submit a claim if:

- directors fail to call meetings or issue resolutions as required by the company's governing documents;
- decisions are made outside the scope of the company's objectives or powers; and

- financial statements or other disclosures are falsified or not made available to shareholders as mandated.

Fraud or Misrepresentation

If the directors or the company mislead shareholders, engage in fraudulent activities or provide false or misleading information (eg, during the issuance of shares or reporting company financial health), shareholders can file a claim against them for damages.

Derivative Actions

Shareholders can bring a derivative action on behalf of the company if directors have engaged in misconduct and the company itself has not taken action to remedy the situation. This allows shareholders to sue for damages arising from the director's breach of duty, fraud or other wrongdoings that harmed the company.

Non-Compliance with Laws and Regulations

If the company or its directors violate Armenian laws or fail to comply with regulations, shareholders may claim damages, especially if the violations harm their financial interests or the company's value.

Shareholder Agreements and Contractual Claims

Shareholders may also bring claims if the company or directors breach specific agreements or contracts made between the shareholders or with the company, such as in cases of unfair buyout terms or non-performance of promises made in shareholder agreements.

Claims for Dividends

If the company fails to distribute dividends to shareholders in line with the law or the company's charter, shareholders may claim the right to receive their share of profits.

Reorganisation or Liquidation Claims

Shareholders may bring claims if the company's reorganisation or liquidation process is conducted unfairly, improperly or in violation of their rights.

Mismanagement or Improper Use of Company Assets

Claims may be brought if directors misuse company assets, engage in excessive spending or otherwise mismanage company resources to the detriment of the shareholders.

These claims may be brought before the courts in Armenia and shareholders generally have the right to seek damages, the removal of directors or the cancellation of unlawful decisions. It is important for shareholders to understand their rights and obligations under Armenian corporate law to effectively pursue these claims.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Legal frameworks in Armenia mandate specific disclosure obligations for shareholders and beneficial owners of publicly traded companies to promote transparency and combat financial malfeasance.

Shareholder Disclosure Obligations

Armenian legislation requires certain entities, such as investment companies, branches of foreign investment companies, regulated market operators, corporate investment funds and investment fund managers to disclose information about their beneficial owners to the CBA. This submission aligns with the standards set by the Law "On Combating Money Laundering and Terrorism Financing" and the requirements established by the CBA's normative legal acts.

Beneficial Ownership Disclosure Obligations

The Law “On Combating Money Laundering and Terrorism Financing” defines a beneficial owner as a natural person who:

- directly or indirectly holds 20% or more of the voting shares or has 20% or more participation in the authorised capital of a legal entity;
- exercises real (factual) control over the legal entity through other means; and
- performs general or current management of the organisation when no individual meets these criteria.

All commercial organisations registered in Armenia, except for LLCs with only natural person participants have to submit declarations of their beneficial owners. Declarations must be submitted electronically to the State Register of Legal Entities within 40 days of the organisation’s registration. Any changes in beneficial ownership information must be declared immediately upon acknowledgment by the organisation and no later than 40 days after the change.

Failure to comply with these disclosure obligations can result in administrative penalties, including warnings or fines. Deliberate concealment or provision of false information may lead to criminal liability. Penalties include deprivation of certain rights or imprisonment.

These regulations underscore Armenia’s commitment to enhancing corporate transparency and aligning with international standards in combating money laundering and terrorism financing.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Companies have to adhere to specific financial reporting and disclosure obligations to ensure transparency and compliance with national regulations. These obligations encompass the preparation and submission of various financial statements, adherence to auditing requirements and timely tax filings.

Annual Financial Statements

All entities must prepare annual financial statements in line with the Armenian Law on Accounting and Financial Reporting.

The standard components of these statements include:

- balance sheet;
- income statement;
- statement of changes in equity;
- cash flow statement; and
- notes on financial statements.

These statements should reflect the financial position of the company as of December 31 of the reporting year. Companies have to submit their annual financial statements to the tax inspectorate.

Audit Requirements

Audits are mandatory for certain categories of entities, including OJSCs, banks and other financial institutions.

The criteria for mandatory audits include the following.

- Public interest organisations and large organisations:

(a) an organisation that:

- (i) is a person making a public offer of securities or a reporting issuer in the territory of Armenia, with the exception of the International Monetary Fund, the European Central Bank, the European Investment Bank, other international organisations which Armenia is a member of, which are persons making a public offer of securities or reporting issuers, or
- (ii) is a bank, credit institution, payment and settlement institution, investment company, regulated market operator, central depository, insurance company, reinsurance company, insurance brokerage company or investment fund manager.

• Medium-sized organisations:

- (a) an organisation that is not a small organisation or a micro-organisation and that, as of the end of the reporting year (for which financial statements must be prepared), has not exceeded at least two of the following three indicators:
 - (i) the total amount of the statement of financial position (balance sheet) – AMD10 billion;
 - (ii) revenue from operations – AMD20 billion; or
 - (iii) the average annual number of employees, calculated in line with the procedure established by the Statistical Committee – 250.

Reporting Deadlines

The fiscal year in Armenia aligns with the calendar year, meaning it ends on December 31 each year. Key reporting deadlines include the following.

Annual financial statements

Due by April 15 of the year following the reporting year.

Corporate income tax returns

Must be filed by April 15 each year, reflecting income earned during the preceding fiscal year.

Quarterly financial reports

These reports must be submitted within 30 days of the end of each quarter.

Penalties for Non-Compliance

Failure to comply with financial reporting and audit requirements can result in fines imposed by regulatory authorities.

Additional Disclosure Obligations

Companies must also disclose changes in management, amendments to articles of incorporation, changes in shareholders and information about ultimate beneficial owners (UBOs). Failure to submit a declaration on UBOs within the prescribed period can result in a warning or a fine. Adherence to these financial reporting and disclosure requirements is essential for maintaining compliance and fostering trust among stakeholders in Armenia's business environment.

6.2 Disclosure of Corporate Governance Arrangements

The disclosure of corporate governance arrangements is governed by the Code of Corporate Governance. The Corporate Governance Code aims to enhance the efficiency of company management, protect shareholder rights and promote transparency and accountability within organisations.

Voluntary Adherence and Reporting Requirements

Adherence to the Corporate Governance Code is voluntary for companies. Organisations that choose to comply are expected to prepare and publish an annual report, which includes a corporate governance report and an annual corporate governance declaration. These documents should be made available on the company's website by June 30 of the year following the reporting period. This approach operates on “*comply or explain*” principle, meaning companies either comply with the Corporate Governance Code's provisions or provide explanations for any deviations.

Legal Framework and Recent Amendments

On 8 June 2024, an amendment to the CC incorporated the Corporate Governance Code into national legislation under Article 76.1. Key aspects of this amendment include:

- the definition of the Corporate Governance Code: the Corporate Governance Code is recognised as a legal act approved by the authorised body responsible for developing investment promotion policies. It contains principles and guidelines aimed at improving the efficiency of company management, safeguarding participant rights and enhancing transparency and accountability; and
- voluntary application: while the Corporate Governance Code is integrated into the legal framework, its application remains voluntary unless otherwise specified by law. Decisions to adopt the Corporate Governance Code are typically made by the general meeting of a company's participants, unless stated differently in legislation or the company's charter.

Implications for Companies

Companies that opt to adhere to the Corporate Governance Code are encouraged to:

- enhance transparency: disclose their corporate governance structures and practices to stakeholders, fostering trust and confidence; and
- aligning with best practices: implement governance principles that align with international standards, potentially attracting foreign investment and contributing to sustainable economic growth.

By voluntarily adopting the Corporate Governance Code and transparently reporting their governance arrangements, Armenian companies can demonstrate a commitment to ethical management and accountability, benefiting both the organisations and their stakeholders.

6.3 Companies Registry Filings

Companies in Armenia are registered with the Agency of the State Register of Legal Entities of the Ministry of Justice.

To register a company, the following documents must be submitted:

- application;
- the decision of the founders on the establishment of a legal entity or the minutes of the founding meeting (congress or other legally established body), which has been signed by all the founders or, in cases provided for by law, the chairman and secretary of the meeting;
- the charter of a legal entity approved by the founder(s) or the founding meeting (congress or other body established by law);
- information about the head of the executive body of the legal entity or their acting duties;

- the sole written decision of the founder if a legal entity is founded by one person;
- the name of the legal entity and the state registration number, if a legal entity is present among the founders of the entity. In addition to the other documents provided, it is also necessary to submit the decision of the authorised body for the management of the founding legal entity and information about the founding legal entity; and
- if the founder of a legal entity established by way of establishment is a foreign legal entity, then for state registration, in addition to the other documents provided, an extract from the commercial register of that country or another similar document confirming the legal status of the foreign legal entity and its constituent documents (or corresponding extracts), certified and translated into Armenian, will also need to be submitted. If the founder of a legal entity established through the establishment is a foreign individual, then for state registration, in addition to the other documents provided, a certified and translated into Armenian copy of the passport or other identity document of the person must be submitted.

These documents are available to the public and are posted in the electronic system of the State Register of Legal Entities of the Ministry of Justice.

If the documents are not submitted properly, the company will not be registered.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

An audit committee attached to the board is formed in an OJSC and the audit committee is

composed exclusively of board members. At least one of the members of the audit committee must be an independent member of the board.

A person who is involved in the management of the current activities of the company and its affiliated person(s) may not be a member of the audit committee.

The chairman of the audit committee will be elected by the board and will be an independent member of the board. The positions of chairman of the board and chairman of the audit committee may not be combined.

The audit committee:

- carries out control (verification) of the process of ensuring the reliability of the company's financial statements and official statements on the financial results of the company's activities;
- carries out analysis of the company's quarterly and annual reports and submits proposals to the board for their approval;
- carries out an audit of the company's internal control function, including risk management, systems for compliance with applicable laws, legal acts and other requirements;
- presents recommendations to the board on the selection criteria, remuneration and other significant conditions of the company's external auditor;
- carries out monitoring and analysis of the independence, objectivity and effectiveness of the company's external auditor;
- meets with the external auditor at least once a year;
- analyses the reports of the company's external auditor and provides relevant information to the board;

- monitors the implementation of the recommendations of the company's external auditor; and
- develops policies on the company's internal control system and monitors their implementation.

The company's charter or internal legal acts may provide the audit committee with other powers.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Directors have to act in the company's best interests and exercise their rights and duties in good faith and with reasonable care, while avoiding actual or potential conflicts of interest. This fiduciary duty encompasses the responsibility for overseeing risk management and internal controls within the company. To promote effective corporate governance, the Armenian government introduced the Corporate Governance Code in 2010, which was updated in 2024. The Corporate Governance Code provides principles and guidelines aimed at enhancing management efficiency, protecting shareholder rights and increasing transparency and accountability.

Incorporating the Corporate Governance Code into company practices can bolster investor confidence, reduce risks and contribute to sustainable economic growth. By aligning with international best practices, Armenian companies can enhance their governance frameworks, thereby supporting long-term success and stability.

In summary, while Armenian law mandates directors to act diligently and in the company's best interests, the Corporate Governance Code offers a structured approach to managing risk and internal controls, encouraging companies to adopt comprehensive governance practices.

Trends and Developments

Contributed by:

Tachat Voskanyan and Artashes Petrosyan
HAP

HAP blends professional experience with the energy of younger talent in its provision of a wide range of legal services. It advises on all aspects of corporate governance and combines deep regulatory knowledge with practical insight into clients' business needs. The firm guides companies, boards, shareholders and executives through complex compliance frameworks, shareholder relations and governance

structures, both in day-to-day operations and during critical transitions. It converts its significant academic knowledge into practical representations of institutional investors in complex insolvency proceedings. During its ten years of practice, the firm has earned its place as an experienced legal services provider in corporate, commercial, administrative law, IT, IP, banking and construction industries.

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Introduction

In the business sector, it is important to have the necessary information about the forms and characteristics of corporate/business organisations. Each organisation has its own distinct features which enable us to choose the right legal entity based on the business sector. In this guide the most frequently used and the most flexible organisations from a business perspective are discussed. The main profit-oriented organisations are the:

- limited liability company (LLC);
- joint stock company (JSC); and
- co-operative.

Features and Characteristics of an LLC

An LLC limits an owner's liability to their investment. It has flexible management and simple registration. The organisation can own property and distribute profits. It requires minimal capital and paperwork. An LLC also offers flexibility and risk protection.

The Court of Cassation of Armenia has described an LLC as an economic company operating through the pooling of shares. In other words, a company in whose activities the degree of participation of a person is determined by the

percentage of that person's share in the total authorised capital.

The number of participants in the company must not exceed 49. If it does, it should be reorganised into an open joint stock company (OJSC) or a commercial co-operative within one year.

The company may be established through the:

- incorporation of a new legal entity; or
- reorganisation of existing companies, such as through a merger, division or transformation in line with corporate law provisions.

The rights of the company's participants are quite broad. They have the right to participate in company management, receive information about the company's activities, receive the designated share of profits etc. At the same time, it should be noted that participants have to make investments in the company's charter capital.

The property of an LLC consists of the investments made by the owners and the property produced and acquired during the company's activities. The company has the right to possess, use and dispose of the property owned by it at its discretion.

An LLC is not liable for its owners' obligations and this gives it the option of creating a business and generating profit without being concerned that the obligations of its owners may be tied to the financial performance of the company.

Individuals wishing to establish a company should conclude a written agreement. The founding document of a company is the charter approved by its founders.

The legislative regulation provides for the alienation of shares. Shares must be sold by a simple written contract and there is no need for notary ratification in alienation.

This option means an LLC is suitable for specific investors, who want to try to make an investment but leave the company easily when it needs to.

Investing in a company is risky. However, if a successful investment is made, an investor can generate profit. From this perspective the law specifies types of settlements which involve share transfers.

Shares in the authorised capital of a company will be transferred to the heirs of citizens and legal successors of legal entities participating in a company, unless the company's charter provides that the transfer is only permitted with the consent of the remaining participants in the company.

It can therefore be stated that, by virtue of this legislative regulation, a shareholder is protected and there is legal certainty that the share yielding profit will subsequently be transferred to their heirs and to their successor in the case of a legal entity.

In many instances, participants in a business may, through their actions or involvement, impede the development of the company. To address this, mechanisms have been put in place to prevent the interference.

The law provides a right to file a lawsuit for the removal of the participants, against owners who hold at least 10% of the company's shares.

This provision effectively ensures the protection of the rights of participants in a company in a court.

On corporate governance issues, the Armenian Code of Civil Procedure contains special provisions that regulate disputes of this kind.

Features and Characteristics of JSCs

JSCs can issue stocks and can generate income through issued stocks. The owner's liability is limited to their investment. There are two types of JSC: OJSC and closed (CJSC).

In an OJSC, owners can sell their shares without the consent of the shareholders. Meanwhile in a CJSC, shares are only issued between shareholders or a predetermined group and other shareholders typically have to approve their transfer.

OJSCs allow for broader shareholders' participation and can raise substantial capital through public stock markets.

This structure enables shareholders to easily sell their shares and leave the company. This model is commonly adopted by large enterprises seeking transparency and openness in management. The number of shareholders in OJSCs is not limited.

Conversely the number of shareholders in a CJSC is limited and the law stipulates that a company must have no more than 49 shareholders.

If the number of shareholders exceeds the statutory limit, the company must take one of the following measures.

- Reorganise as an OJSC, in compliance with the applicable corporate regulations.
- Reduce the number of shareholders to meet the legal threshold.

Failure to comply with either measure may result in liquidation by court order.

The shareholders of a CJSC have a pre-emptive right to acquire shares sold by other shareholders.

If a shareholder does not exercise this right within the charter's timeframe, the company may acquire the shares at an agreed price. If the company declines or disagrees on price, the shares may be sold to a third party.

For JSCs, the public issuing of stocks is carried out by the Armenian Stock Exchange (the "AMX"), which is the operator of the regulated securities market in Armenia. It enables the execution of shares, government and corporate bonds, foreign exchange, repo agreements and currency swaps through its automated platforms.

To understand the main features of a JSC it is necessary to discuss the management of this type of company.

The supreme management body of a JSC is the general meeting of shareholders (the "GSM").

The GSM of a JSC has the power:

- to amend the charter and authorised capital;
- elect members of the company's board of directors (BoD) and audit committee (auditor);
- terminate the BoD' and auditor's powers early;
- form executive bodies of the company and terminate their powers early;
- approve the company's annual reports; and
- make a decision to reorganise or liquidate the company.

The GSM is therefore the supreme governing body of a JSC. It defines strategy, approves financial reports and elects executives. Its distinctiveness lies in its exclusive power to amend the company's charter and to facilitate the dissolution of the company.

A BoD is established in a company with more than 50 shareholders. When establishing a BoD its jurisdiction must be defined by the company's charter.

The executive body of the company may be collegial (board, management) or sole (director, general director). The executive body manages the current activities of the company and is accountable to the BoD and the GSM.

The JSC model enables owners to manage a company through a general meeting of a JSC and provide ongoing management at the same time.

The law stipulates two types of shares: common (ordinary) and privileged. The owner of a common (ordinary) share has the right, in line with the law and the charter to participate in the meeting and vote on all issues within its jurisdiction. Meanwhile, the management of the company

receives dividends from the profits generated by the company's activities. At the same time holders of preferred shares do not have the right to vote at the meeting, unless otherwise provided for by the law and the charter for certain classes of preferred shares.

In the business sector these two types of shares suggest a variety of possibilities. If a business maker only wants a profit from the company's activities and is not interested in managing, a dividend is more suitable than privileged shares. However, when it necessary to also join in the management of a company, holding common (ordinary) shares is a more suitable way.

There is also a clarifying regulation on the share agreement. This regulation allows shareholders to take particular co-ordinated actions or even refrain from taking these actions.

For example, the shareholders' agreement can cover:

- the obligation to vote at the GSM in the way specified by the agreement;
- the voting procedure or voting with other people; or
- voting on the instructions of other people, to acquire shares at a pre-determined price etc.

A new regulation has also been developed for companies that allows investors to attract certain funds to the company's capital at the expense of the investor's funds.

This type of agreement is called a simple agreement for future equity (SAFE). It establishes a commitment from one party, typically the investor, to contribute a specified amount of financial resources to the company. In return, the company agrees to issue and allocate shares of a specified

quantity, type and class, as stipulated in the agreement, once the conditions set out in it are met.

This legislative regulation is suitable for those companies who want to use financial resources and generate some profit.

The legislative regulation provides an opportunity to secure financial resources upfront while fulfilling obligations laid out in the contract.

A JSC also may allocate shares to employees in line with its charter or an employee share ownership plan approved by the GSM. These plans regulate the acquisition, use, transfer and buy-back of shares, providing JSC's with a tool to incentivise and retain key personnel.

Features and Characteristics of Co-operatives

Profit-seeking organisations in Armenia can also be co-operatives, which is an association of individuals and legal entities.

Its primary purpose is to meet the material or other needs of its members, which is achieved by pooling their resources, specifically through financial contributions.

The main characteristic of a co-operative is that it is based on both the membership of individuals (legal entities) and their financial contributions, which means that unlike LLCs or JSCs, which have no participation and are based on the shares of participants and dividends, a co-operative is solely focused on profit distribution. A co-operative also imposes a participation fee and meets the material or other needs of its members.

As a commercial entity, a co-operative operates on the principle of achieving economic goals to serve the interests of its members.

While the primary aim of a co-operative is to improve the welfare of its members by meeting their needs it also functions as a commercial organisation, operating in the market and engaging in entrepreneurial activities.

Like any commercial organisation, a co-operative seeks to generate financial income, which is distributed based on the members' participation fee.

The Armenian Civil Code stipulates the regulation of legal relations related to the property of the co-operative.

A member of a co-operative is obliged to pay the share premium in full before the co-operative can be registered.

If losses are incurred through additional payments, the members of the co-operative are obliged to cover them. However, the law also obliges the members to pay the participation fee of other members, where there is a failure to fulfill this obligation.

The supreme governing body of a co-operative is the general meeting of its members (the "GMM"). The GMM has exclusive jurisdiction to:

- amend the co-operative's charter;
- form a supervisory board;
- terminate the powers of its members;
- admit and dismiss members of the co-operative; and
- approve the co-operative's annual reports.

At the same time legislative regulations specify a supervisory board must be established. This will exercise control over the activities of the co-operative's executive bodies if the co-operative has more than 50 members.

The law gives members the option to withdraw from the co-operative. If they do withdraw, the value of their share will be paid to members or given property corresponding to it.

At the same time, members may be expelled from the co-operative following a decision of the GMM if they have failed to fulfill or improperly fulfilled obligations.

The co-operative may be voluntarily reorganised or dissolved by a decision of the GMM.

A commercial co-operative facilitates the creation of an organisation where members can jointly engage in commercial activities, enabling the generation of economic profits, while enhancing organisational efficiency through the collaboration of resources, workforce or other joint initiatives. A co-operative is suitable for businesses where members can pool investments, utilise technologies, infrastructure or supply chains, thereby increasing competitiveness and reducing costs.

The main advantage of a co-operative lies in the joint use of resources, which provides an economic benefit and greater control over the organisation's operations.

However, it is important to consider the risks, particularly the legal limitations of liability.

Conclusion

This guide has outlined the primary characteristics of the main corporate and business organisations. Each business has its own characteristics and depending on the form of the business, it is essential to select the type and structure of the organisation carefully and appropriately to ensure the development of the business can be supported in the best possible way.

BAHRAIN

Law and Practice

Contributed by:

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Hassan Radhi & Associates is one of the largest and most reputable leading law firms in Bahrain and in the Gulf region. The office was founded in 1974 by Dr Hassan Ali Radhi, the senior partner of the firm, and has more than 50 years of legal experience and professionalism in the legal sector, especially in banking, finance and corporate law. The firm has a team of highly qualified lawyers, supported by a dedi-

cated and professional administrative team that provides exceptional legal services, locally and internationally, in Arabic and English. As part of the Lex Mundi global network, HRA is the only member firm in Bahrain and can provide its clients with access to more than 21,000 lawyers around the world with in-depth experience in 100-plus countries worldwide, all from a single point of contact.

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حسن رضي ومشاركوه
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1. Introductory

1.1 Forms of Corporate/Business Organisations

Persons choosing to conduct business in Bahrain may choose from a variety of business structures set out in the Commercial Companies Law (CCL) promulgated by Decree Law No (21) of 2001, which is amended periodically.

The most common types of business entities in Bahrain are limited liability companies, public joint stock companies and closed joint stock companies. All are entities in which the shareholders' liability towards creditors is limited to their shareholding in the capital (ie, limited liability).

Limited Liability Companies

Limited liability companies are companies with a minimum of one partner, who is responsible only to the extent of the shareholding in the capital. Partners may not resort to public subscription for raising shares or loan capital. This type of company is barred from undertaking insurance activities, banking or the investment of funds for the account of third parties (shareholders of this kind are referred to as "*partners*").

The company is not required to have a board of directors unless the number of partners exceeds ten.

Joint Stock Companies

Other types of company include the following:

- a closed joint stock company is established with a minimum of two shareholders and a minimum share capital of BHD50,000 (around USD132,625) – the shares of the company may not be publicly offered; and
- a public joint stock company is established by a number of persons who subscribe to it via negotiable shares.

The latter form is subject to a minimum share capital of BHD1 million (around USD2.6 million). The minimum number of shareholders is two, with the exception of companies formed by the government or in which the government is associated in the formation thereof.

General Partnerships/Simple Commandite Partnerships

Less regulated types of business entities are general partnerships companies and simple commandite partnerships.

- A general partnership company is owned by two or more persons whose liability is unlimited and who are jointly and severally liable to cover the company's debts and commitments. The company's name consists of the name of one or more of the partners with the addition of "and Co" to indicate the partnership.
- A simple commandite partnership is one which is established by two types of partners: joint partners and sleeping partners.

Regarding a commandite partnership, joint partners are those who are involved in the management of the company and have unlimited liability towards creditors. Sleeping partners are not involved in the management of the company and are only liable for the obligations of the company to the extent of their shareholding in the capital.

Branches of Foreign Companies

Another form of business entity is a branch of a foreign company, which must be guaranteed by the head office of the company. The activities of a business entity licensed as "branch" shall match the activities of the head office. Branches licensed as a representative office are limited to gathering financial, economic and commercial information, carrying out general promotional activities and providing general assistance of a non-specific nature to customers of its parent company.

Holding Companies

Holding companies are very common in Bahrain. They may be in the form of a public or private joint stock company, or a limited liability company. The role of holding companies is limited to the investment of funds, ownership of shares in its subsidiaries, management of its subsidiaries and the provision of financing or guarantees for its affiliates.

Commercial Companies

Commercial companies are mainly governed by the CCL and may be subject to other laws and regulations depending on the nature of their activity. Most importantly, companies licensed to provide regulated financial services by the Central Bank of Bahrain (CBB) are subject to the laws and regulations concerning the regulated services.

1.2 Sources of Corporate Governance Requirements

The main legislations related to corporate governance that must be observed by companies incorporated in Bahrain are as follows.

The CCL

The CCL is the law governing commercial companies, their types, formation and management. The CCL has been in force since 2001 and has subsequently been amended, with the latest amendment issued in September 2021. It includes rules related to the segregation of powers and scope of powers of the board of directors and the shareholders, as well as accountability and cases of personal liability.

Rules relating to disclosure of interests by board members and avoidance of conflict of interest are included in the CCL.

The Corporate Governance Code

The Corporate Governance Code was issued by Decision No (19) of 2018 by the Minister of Industry and Commerce pursuant to Article 358 bis of the CCL. This code provides the minimum required standards for corporate governance and applies to all joint stock companies incorporated in Bahrain, with the exception of companies carrying out regulated financial services and licensed by the Central Bank of Bahrain, which

are subject to a designated corporate governance code.

This code includes 11 main corporate governance principles as follows:

- the board shall be effective, qualified and have the required expertise;
- the directors and executive management shall have full loyalty to the company;
- there must be rigorous controls for financial audit and reporting, internal control and compliance with the law;
- the requirement for effective procedures for appointment, training and evaluation of the directors;
- fair and responsible remuneration for directors and senior officers;
- the requirement of a clear and efficient management structure with defined job titles, powers, roles and responsibilities;
- shareholder involvement by encouraging communication and participation;
- disclosure of companies' corporate governance;
- for companies that offer Islamic services, adherence to the principles of Sharia;
- integrity of the financial statements and the importance of external auditors as a responsibility of the board; and
- social responsibility.

Boards of joint stock companies, closed and public, are required to form a corporate governance committee to appoint a corporate governance officer to ensure compliance with the corporate governance rules and submit a corporate governance report annually to the Ministry of Industry and Commerce, setting out each principle and the measures taken to comply therewith, with a special section for related-party transactions.

The principles of the Corporate Governance Code are advised to be observed by all types of companies, including limited liability companies. The reporting requirements, however, are enforced on closed and public joint stock companies.

The Rulebook of the CBB

The Corporate Governance Code is embedded in the High-Level Control Module of the Rulebook of the CBB applicable to each category of CBB licensee. This is issued by the CBB and the compliance therewith is supervised by the CBB.

This code includes the first nine principles of the Corporate Governance Code listed above.

Constitutional Documents

The memorandum and articles of association of a company (the "*Constitutional Documents*"), produced by the company's shareholders, provide company-specific rules that include the authority of the board, the extent of its powers, its duties and remuneration.

Rules, Regulations and Circulars

The rules, regulations and circulars by the CBB and the Bahrain Bourse (the company taking over the powers of the Bahrain Stock Exchange) applicable to listed companies (all public companies and some listed closed companies) are detailed in **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Within the CCL, the provisions for each type of company are included in a separate chapter. The chapter relating to the management of public joint stock companies includes the most

and more stringent rules. For example, the rules relating to the board of directors require a minimum of five directors that must include independent and non-executive directors, director appointment and election rules, the requirement to have an audit committee within the board and the limitation on director remuneration in the years when no dividends are to be paid to the shareholders.

The rules under the CCL are mandatory.

The Corporate Governance Code applies to all types of companies, with an emphasis on the importance of compliance especially by joint stock companies due to the role they play in the national economy. Compliance with the principles of the Corporate Governance Code is on a comply-or-explain basis and the standard applied by the Ministry of Industry and Commerce for listed and public joint stock companies is higher than that applied to the other forms of companies.

In addition to the CCL and Corporate Governance Code, additional rules by the CBB and the Bahrain Bourse are put in place for listed companies, of which the following include provisions related to corporate governance.

The Bahrain Bourse Listing Rules

These Listing Rules were approved by Board of Directors Resolution (3/5/2024) in its Meeting (5/2024) dated 30 September 2024. Their purpose is to set out the requirements that must be complied with by all applicants, issuers, their directors, officers, advisers or other persons to whom these Listing Rules are directed. The Listing Rules are composed of both requirements that have to be met before securities may be listed and also continuing obligations that an issuer must comply with after listing.

The principles on which these Listing Rules are based include the following:

- issuers shall have acceptable standards of quality, operations, management experience and expertise;
- investors and their professional advisers shall be kept fully informed by the issuer of all facts and information that might affect their existing or potential interests in the issuer – in particular, full, accurate and timely disclosure shall be made of any information which may reasonably be expected to have a material effect on the price, value or market activity in the securities of issuers;
- all holders of any class of securities will be treated fairly and equitably;
- directors, officers and advisers of issuers will maintain the highest standards of integrity, accountability, corporate governance and responsibility; and
- directors of an issuer shall act in the interests of shareholders as a whole.

The Disclosure Standards by the Bahrain Bourse

Disclosure Standards were issued by Bahrain Monetary Agency (now known as the Central Bank of Bahrain) pursuant to its circular dated 3 December 2003. Except for the First Chapter, which is superseded by the Offering of Securities Module under Rulebook 6, the Disclosure Standards still apply to listings, public offerings and sales of securities in Bahrain. The Disclosure Standards contain, inter alia, guidelines for trading by directors and senior management and policy on immediate public disclosure of material information regarding an issuer's affairs, or about events or conditions in the market that will affect the issuer's securities, relating to the business that would significantly affect the market price or value of any of the issuer's securities,

or that would reasonably be expected to have a major influence on any investor's decisions.

The Offering of Securities Module Issued by the CBB

This Module contains the CBB's Directive (as amended from time to time) relating to the issuing and offering of securities. The directive in this Module is applicable to all market participants and relevant persons, including but not limited to: issuers of securities or any person acting on their behalf, listed companies, any person acting for or on behalf of listed companies, and shareholders of listed companies.

This Module describes, among other things, the eligibility criteria for issuing securities and the application procedures for obtaining the regulator's approval. Most importantly, it explains the requirement for companies to prepare a prospectus or offering circular when they offer their securities to the public or on private placement basis. The directors of the company must accept responsibility for the accuracy of the content of such prospectus or offering circular.

The Takeovers, Mergers and Acquisitions Module by the CBB

This Module applies to persons involved in, engaging in or intending to engage in an offer for, takeover or merger or acquisition of a controlling interest (30% or more) in a company whose primary listing of its ordinary equity securities is on a licensed exchange in Bahrain. Each director of an offeror and of the offeree company, as well as those acting in concert and their professional advisers, has a responsibility to ensure, so far as they are reasonably able, that the requirements of the Module are complied with in the conduct of transactions subject to it.

While this Module applies to listed companies in which control may change as mentioned above, there are circumstances, such as where an unlisted company is a target of a listed company (reverse takeover), in which it is necessary to consider the spirit, general principles, standards and rules of this Module wherever it is applicable. When there is any doubt as to whether a proposed course of conduct accords with the spirit, general principles, standards and rules of this Module, parties or their advisers should consult the CBB in advance.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

The market is closely monitored by the Ministry of Industry and Commerce, the Bahrain Bourse, and the CBB through the various directorates under its umbrella. As a result of close monitoring, regulations, circulars and directives are issued on a regular basis, focusing on transparency, efficiency, clear communication, fairness, accountability and anti-money laundering.

2.2 ESG Considerations

Companies with activities that are environment-related are subject to the rules and regulations governing this sector and are required to adhere to the laws on Environment and Public Health as well as the regulations and standards of the Supreme Council for Environment. Ensuring compliance with the law is good governance and is the responsibility of the company and its board of directors.

Social responsibility is one of the principles of corporate governance detailed in **1.2 Sources of Corporate Governance Requirements**. Companies are considered to have social responsibility and the board of directors is expected to have

a code in place which sets out the requirements of social responsibility of the company. A report on activities undertaken in this respect shall be included in the company's annual report.

Generally, companies make voluntary contributions to the environment as part of their social responsibility.

The CBB has issued the Environmental, Social and Governance Requirements Module (the “ESG Module”) in November 2023, which requires listed companies and CBB licensees to submit an ESG report to the CBB on an annual basis.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The management of the company is the role of:

- the board of directors in joint stock companies, including the committees formed within the board;
- the board of managers in limited liability companies; and
- the general meeting of the shareholders (ordinary and extraordinary, as detailed in **5.3 Shareholder Meetings**).

The powers of the board of managers in limited liability companies pursuant to the CCL are determined by the company's Constitutional Documents.

The board of directors of joint stock companies has the power to run the management of the company subject to certain restrictions that specifically require the approval of the general

meeting of the shareholders, as detailed in **3.2 Decisions Made by Particular Bodies**.

Boards of joint stock companies are required to form an audit committee from amongst the members of the board. The audit committee shall have the mandate of reviewing the audit, accounting and financial practices of the company, and the extent of compliance with the provisions of the law and the Constitutional Documents. To fulfil its mandate, the audit committee shall be able to access all of the company's records, documents and information, and shall submit a report of its work in the annual report to the shareholders.

The Corporate Governance

The Corporate Governance Code requires the companies subject to its provisions to set up audit, remuneration, nomination and corporate governance committees from amongst the board members as required by the Code, and allows the board to decide on setting up additional specialised committees as required by the activities of the company:

- the audit committee is in charge of reviewing the company's audit, financial and accounting procedures and ensuring compliance with the law and the company's Constitutional Documents;
- the remuneration committee is in charge of reviewing and setting the basis for remunerating directors and senior managers;
- the nomination committee is in charge of making nominations and recommendations for directorship and senior management positions in the company. It is also in charge of reviewing the independence criteria and status of directors on an ongoing basis – this committee may be merged with the remuneration committee and usually is; and

- the corporate governance committee is in charge of reviewing the company's corporate governance policy and making recommendations to ensure compliance – this committee may be merged with the nomination and remuneration committee.

3.2 Decisions Made by Particular Bodies

The board of directors of a joint stock company has the authority, by law, to do all actions necessary for the management of the company in accordance with its objectives, except as restricted by law, the Constitutional Documents or general meeting resolutions.

The CBB Rulebook provides more detailed guidance on the role of the board, but this guidance can apply to all companies. This role includes setting the overall business strategy of the company, ensuring that financial statements are prepared in a manner that accurately reflects the company's financial position, monitoring management performance, convening and preparing the agenda for shareholder meetings, monitoring conflicts of interest and preventing abusive related party transactions and assuring equitable treatment of all shareholders, including minority shareholders.

Unless allowed by a company's Constitutional Documents, the board shall not have the power to issue securities, conclude loans for more than three years, sell the company's assets or business, mortgage such assets, provide guarantees for third parties, discharge the company's debtors from their liabilities, reach a settlement in respect thereof or donate the company's assets without approval of the general meeting of the shareholders unless such actions fall within the essence of the company's objectives.

The shareholders participate in the management of the company through general meetings. There are two types of general meetings, each with a defined scope of powers, as detailed in 5.3 **Shareholder Meetings**.

3.3 Decision-Making Processes

The Shareholders

The shareholders are required to hold one ordinary general meeting within three months from the end of the fiscal year, and an extraordinary general meeting whenever required. The details of the process of each type of meeting are found in 5.3 **Shareholder Meetings**.

The Board

In joint stock companies, the following apply.

- A board is required to meet at least four times a year, by invitation from the chairman of the board (the "*chairman*") or at least two directors; the board issues resolutions for the management of the company.
- The quorum for the meeting is half the number of directors, subject to a minimum of three, unless a higher amount is required in the Constitutional Documents.
- There shall be no attendance by proxy unless allowed by the Constitutional Documents. Decisions are issued by a majority vote of the directors in attendance. In case of a tie, the chairman shall have the casting vote.
- Any director who objects to a decision must minute their objection. If a case is lodged against the board on the basis of a decision with negative outcome, the minutes will serve to absolve the objecting director of liability.
- Meetings of the board may be attended by video or teleconference if the Constitutional Documents allow.

- Decisions may be issued by circulation if the Constitutional Documents of the company allow for the same.

Regarding the third bullet point, only a director or representative of a corporate shareholder may hold the proxy for a board meeting. A maximum of two directors may attend by proxy, and at least half the directors must attend in person, including the chairman, for the meeting to be valid, subject to a minimum of two in closed companies and three in public companies.

4. Directors and Officers

4.1 Board Structure

Companies With Limited Liability

Companies with limited liability may be managed by the partners or a manager or board of managers appointed by the partners. A board of managers is not required unless the number of partners exceeds ten. The formation of the board of managers and its powers shall be set out in the Constitutional Documents.

Closed Joint Stock

Closed joint stock companies are managed by a board of directors with a minimum of three directors and a maximum of 15 directors, a maximum term of three years, and renewable by the general assembly.

The boards of closed joint stock companies that are listed in the Bahrain Bourse must include independent and non-executive directors. The Minister of Industry and Commerce and CBB may issue decisions to include more categories of closed joint stock companies to which this requirement is to apply.

Public Joint Stock

Public joint stock companies are managed by a board with a minimum of five directors and a maximum of 15 directors, a maximum term of three years, and renewable by the general assembly. The board must include independent and non-executive members.

The board of directors of joint stock companies must choose a chairman and vice-chairman from its members by way of secret ballot. The Ministry must be informed of the decision.

For CBB licensees, the chairman is required to be an independent member and must be approved by the CBB for that position.

The board of directors of public companies and some closed companies must form committees from amongst its members as set out in **3.1 Bodies or Functions Involved in Governance and Management** and **6.2 Disclosure of Corporate Governance Arrangements**.

Companies licensed by the CBB are subject to the independence requirements set out in the applicable Rulebook volume for their type of licence.

4.2 Roles of Board Members

The Chairman

The chairman is considered the head of the company. The chairman represents the company before third parties and their signature solely shall bind the company in its relationship with third parties, unless the Constitutional Documents require the chairman to have joint signature authority with one director or more. The chairman must ensure that the decisions of the board are executed.

The Vice-Chairman

The vice-chairman shall take the role of the chairman in their absence.

The Directors

Jointly, the directors must fulfil the role of the board in the management of the company. Severally, each director must ensure that they work in the best interest of the company and make the decisions and actions required to serve that interest.

In addition to the committees within the board, the roles are set out in **3.1 Bodies or Functions Involved in Governance and Management**.

4.3 Board Composition Requirements/Recommendations

The composition of the board of directors is as set out in **4.1 Board Structure**.

The board of joint stock companies must include independent and non-executive directors, and may also include non-independent and executive directors as detailed in **4.5 Rules/Requirements Concerning Independence of Directors**.

In the case of CBB licensees, half of the board of directors, including the chairman, are required to be independent.

4.4 Appointment and Removal of Directors/Officers

Directors are nominated by appointment or election by the general meeting of the shareholders. The general meeting of the shareholders is the authority with director removal powers.

Pursuant to the CCL, any shareholder owning at least 10% of the capital of the company has the right to appoint a director, subject to the size of the board and the requirements of director-

ship and approval requirements in case of CBB licensees.

Shareholders not eligible to appoint or those who do not choose to appoint a director may use their percentage to elect directors by cumulative voting.

There are generally no restrictions to appointment but general guidelines set out in the CCL are as follows:

- having legal capacity to act;
- not having been convicted of a crime involving negligent or fraudulent bankruptcy or a crime related to honour, breach of trust or violation of the provisions of the CCL, unless reinstated;
- not being prohibited from being a director in a joint stock company pursuant to the CCL or any other law in force in Bahrain;
- the restriction on the Chairman and Deputy Chairman holding the same position as the most senior executive in the company;
- special independence conditions for directors of CBB-licensed companies; and
- these are in addition to any restrictions stipulated in the memorandum and articles of association of the company.

4.5 Rules/Requirements Concerning Independence of Directors

Independent directors are those that are deemed by the board to be independent of any specific shareholder and who do not have any significant business interest with the company.

Non-independent directors are those who represent a shareholder or those who have a business interest with the company. A director is considered non-independent if they:

- hold 10% or more of the shares of the company, the parent company, or any of its subsidiaries or associates;
- represent a legal person who holds 10% or more of the shares of the company, parent or any of its subsidiaries or associates;
- served in an executive position in the company, its parent or any of its subsidiaries or associates, in the two years preceding their nomination;
- are a first-degree relative of an existing director or any person in a key executive management position in the company, its parent, or any of its subsidiaries or associates;
- are a director of the company's parent or any of its subsidiaries or associates;
- were employed by any of the company's contracting parties such as external auditors, major suppliers, etc, in the two years preceding their nomination;
- were employed by the parent company or any of its subsidiaries or associates in the two years preceding their nomination;
- have made or received payment from the company in the value of over BHD50,000 (around USD132,625), apart from directors' remuneration if they are an existing director in the past year;
- are a relative of a partner in the company's external auditor or an employee thereof, or has been in the past two years; or
- are an employee or partner at a company that provides consulting services to the company, its parent, or any of its subsidiaries and associates (this does not apply if the parent company is owned at least 75% by the government or is a government entity).

Executive directors are those who hold senior management positions within the company. Executive directors are not considered independent.

Non-executive directors are those who are not involved in the day-to-day management of the company or a controller of a company, subsidiary or affiliate thereof.

4.6 Legal Duties of Directors/Officers

The legal duties of directors of a company may be summarised as follows:

- to participate in the management of the company in a diligent, skilful and efficient manner in accordance with the law and the Constitutional Documents;
- to serve the company as a representative of the interests of all the shareholders, and not one or a specific group of shareholders; and
- to disclose any personal interest they may have in any of the issues discussed in board or general meetings and to refrain from voting in respect of any of these issues.

4.7 Responsibility/Accountability of Directors

Once a director is on the board, they owe a duty towards all the shareholders, and the interests of all the shareholders must be considered.

However, any stakeholder affected by any decision of the board or a director has the right to lodge a claim at court in accordance with Article 185 and 18 bis of the CCL (detailed in 5.4 Shareholder Claims).

4.8 Consequences and Enforcement of Breach of Directors' Duties

The consequence of a breach of directors' duties includes dismissal from office, and possibly a claim at court in accordance with Article 18 bis of the CCL (as detailed in 5.4 Shareholder Claims).

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Directors, officers and even shareholders may be held personally liable without limitation if any of the breaches listed under Article 185 and Article 18 bis of the CCL (see 5.4 Shareholder Claims) are proven.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The Constitutional Documents of a company may set out the procedure and requirements for determining the remuneration of the directors, subject to a maximum remuneration of 10% of the net profit after deducting legal reserves and distributing dividends not less than 5% of the company's paid-up capital.

In the years where no dividends are paid to the shareholders, the company is prohibited from paying remuneration to the directors, unless the specific approval of the Minister of Industry and Commerce for such payment is obtained. In case of CBB licensees, the CBB must approve the payment and value of remuneration to the directors.

A detailed report on all payments made to the directors and executive management in a fiscal year must be prepared by the board and submitted to the shareholders. This must detail any and all payments, including salaries, sitting fees, representation fees, allowances, etc. Failure to submit the report subjects the directors to liability that may include personal liability for failure to comply with the law.

4.11 Disclosure of Payments to Directors/Officers

Information on the remuneration, fees or benefits payable to each of the directors and officers is

required to be submitted to the general meeting of the company's shareholders.

Public disclosure of such information is only required in case of offering of securities pursuant to the CBB's Offering of Securities Module.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The Constitutional Documents of a company (Memorandum and Articles of Association) bridge the relationship between the shareholders and the company. Drafted within the frameworks of the CCL, they describe the rights and obligations of the shareholders towards the company.

The inherent rights and obligations of the shareholders include the following:

Rights:

- receiving profit or dividends decided for the shareholders;
- receiving a share of the company's total property upon liquidation;
- participating in the company's management, whether through the general assemblies or as a member of the board of directors, according to the company's constitutional documents;
- obtaining a printed booklet comprising the company's balance sheet for the past fiscal year, the profit and loss account and the reports of the board of directors and the auditor; and
- filing lawsuits to nullify any decision issued by the general meeting or by the board of directors in violation of the law, the public order or the constitutional documents of the company.

Obligations:

- payment of accrued instalments and delay interests following the expiration of the date thereof without the need for serving a notice upon them;
- payment of expenses incurred by the company in collecting unpaid instalments and sale of shares;
- refraining from any action intended to cause harm to the company; and
- execution of any decision legally passed by the general meeting.

5.2 Role of Shareholders in Company Management

The general meeting of the shareholders is the ultimate decision-making authority in the company.

The company's Constitutional Documents specify the extent of the board of directors' powers in the company. Some decisions require the approval of the general assembly, such as the decisions set out in **3.2 Decisions Made by Particular Bodies**.

The involvement of shareholders in the company's management and participation in controlling the activities of the directors is through their participation in the general meetings and the decisions made therein.

5.3 Shareholder Meetings

There are two types of general meetings of the shareholders of a company – an Ordinary General Meeting and an Extraordinary General Meeting – each with different scope of powers. To ensure that all shareholders are allowed the same opportunity to participate in the general meetings, there are specific provisions regarding invitation to the meetings.

Ordinary General Meeting

The Ordinary General Meeting of shareholders convenes at the invitation of the chairman of the board of directors at the time and venue specified in the company's constitutional documents. The meeting must convene at least once per year during the three-month period following the end of the company's fiscal or financial year in case of listed companies and companies licensed by the CBB, and during the six-month period following the end of the company's financial year for companies not listed on the Bahrain Bourse or licensed by the CBB. The invitation to convene the Ordinary General Meeting of shareholders must be sent to the shareholders, and in the case of a public joint stock company, the invitation is required to be published in at least two daily local newspapers and one of them at least to be in Arabic and the other in English.

The minimum notice period is 21 days and the notice of the meeting must include the agenda of the meeting. Copies of the invitation documents must also be forwarded to the Ministry of Industry and Commerce at least ten days before the Ordinary General Meeting. The Ordinary General Meeting is presided over by the chairman of the board of directors or their deputy or whoever is delegated by the Ordinary General Meeting.

Validity

The Ordinary General Meeting shall not be valid unless it is attended by a number of shareholders who have the right to vote and representing more than half the capital of the company. If this quorum is not attained, an invitation is required to be sent for a second meeting to be held for the same agenda within seven to 15 days from the date fixed for the first meeting.

Second and third meetings

The second meeting shall not be valid unless it is attended by a number of shareholders who have the right to vote and representing more than at least 30% of the capital of the company.

The third meeting shall be valid regardless of the number of shareholders present. Each shareholder, regardless of the number of their shares in the company, shall have the right to attend the Ordinary General Meeting, and shall have a number of votes equal to the number of their shares. Any provision or decision to the contrary shall be deemed null and void.

Delegates and representatives

Any shareholder may delegate a person, from among the shareholders or third parties, to attend the Ordinary General Meeting on their behalf, provided that this person is not the chairman of the board or a board member or an employee of the company. However, this shall not prejudice the right to delegate a first-degree relative by virtue of a written special power of attorney, to be prepared by the company for this purpose.

Members lacking capacity or incapacitated (for instance, minor or person with unsound mind) shall be represented in the meeting by their legal representatives.

Extraordinary General Meeting

The Extraordinary General Meeting convenes at the invitation of the board of directors or by virtue of a written request addressed to the board of directors by a number of shareholders representing at least 10% of the company's capital.

Validity

The Extraordinary General Meeting shall not be valid unless attended by shareholders represent-

ing at least two thirds of the company's capital. If this quorum is not present, a second meeting shall be invited within 15 days following the first meeting. The second meeting shall be valid if attended by shareholders representing more than one third of the capital.

If such quorum is not available at the second meeting, a third meeting shall be convened within 15 days from the date of the second meeting. The third meeting shall be valid if attended by a quarter of the shareholders. A new invitation is not required to be sent for the last two meetings if their dates have been specified in the invitation to the first meeting, provided that publication is made in at least two daily local newspapers – one of them must be in Arabic and the other in English – to the effect that none of these meetings has occurred.

Decisions

The decision of the Extraordinary General Meeting shall be passed by a two-thirds majority of the shares represented at the meeting, unless the decision relates to the increase or decrease of the company's capital, the extension of the company's term, dissolution, conversion or merging thereof with another company, in which case it shall not be valid unless passed by a three-quarters majority of the shares present at the meeting and with whose attendance the meeting is considered valid. The Extraordinary General Meeting's decisions shall become effective upon the approval of the Ministry of Industry and Commerce.

Other

In addition to the above, the founders shall invite the constituent assembly to convene within a period no later than 21 days from the date of the closing of the subscription (in case of public joint stock company) and seven days from the date

of the incorporation approval by the Ministry of Industry and Commerce (in case of closed joint stock company).

The invitation to convene the constituent assembly of shareholders shall be published in at least two daily local newspapers – one of them at least to be in Arabic and the other in English. The minimum notice period is 21 days and the notice shall include the agenda of the meeting. Copies of the invitation documents shall be forwarded to the Ministry at least ten days before the meeting.

5.4 Shareholder Claims

The bases of claim that exist for shareholders against the company are as follows:

- a shareholder may lodge a claim seeking to nullify a decision by the general meeting if such decision is not issued in accordance with the law and the Constitutional Documents of the company;
- pursuant to Article 168 bis of the CCL, a shareholder may lodge a claim against the company if its business is being conducted in a manner that unfairly causes damage to the shareholders or a group of shareholders, or if the company intends to take an action that causes damage to the shareholders or a group of shareholders; and
- pursuant to Article 18 bis of the CCL, a shareholder may lodge a claim against any officer, director or even another shareholder, on the basis of the following:
 - (a) providing incorrect information about the company's capital in any document likely to affect the company's financial standing;
 - (b) using the company for fraudulent or illegal purposes;
 - (c) using the company's assets as if they are their own;
 - (d) conflict of interest;

- (e) making decisions or taking actions that encumber the company with obligations knowing that the company cannot fulfil, or if the company is unable to fulfil its obligations as a result of an officer, director or shareholder's gross negligence or error;
- (f) if their decisions and actions cause the company to be unable to pay taxes or official fees;
- (g) violation of the provisions of the law or company's constitutional documents;
- (h) the limitation of powers is not observed or duties are performed in a fraudulent or gross negligent manner; and
- (i) failure to act as a prudent, reasonable person in a given circumstance.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Any person whose ownership, in a publicly traded company, alone or their ownership together with that of their minor children, or any other accounts under their disposal, or the ownership of any of their associate or affiliate companies, amounts to 5% or more of any listed security of a joint stock company, must notify the licensed exchange (Bahrain Bourse) forthwith, which shall in turn notify the CBB of this fact and the CBB may declare the name of the person who owns such stake.

All persons must obtain a CBB prior written approval to execute any order that will bring their ownership alone or their ownership together with their minor children, or the accounts standing under their disposal, to 10% or more in any listed security. Any further increase of 1% or more shall also be subject to CBB prior written approval.

Companies are further required to disclose ultimate beneficial owner information to the Ministry of Industry and Commerce.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Limited liability companies, branches of foreign companies and joint stock companies are required to submit the audited financial statements of the company to the Ministry of Industry and Commerce.

Joint stock companies shall annually prepare a detailed list, approved by the chairman and the managing director, if any, of the names and capacity of the chairman and members of this board, and the managers of the company. The company shall keep a copy of this list and the original shall be sent to the Ministry of Industry and Commerce accompanied by the annual report prepared by the board of directors, the company's balance sheet and the profits and losses account.

Companies licensed by the CBB must submit the reports to the CBB in accordance with the Rulebook volume applicable to its type of licence. The CBB has issued the Environmental, Social and Governance Requirements Module (ESG Module) in November 2023, which requires listed companies and CBB licensees to submit an ESG report to the CBB on an annual basis.

6.2 Disclosure of Corporate Governance Arrangements

Joint stock companies are required to disclose their corporate governance, which may be achieved by fulfilling the following requirements.

- The board shall adopt written corporate governance guidelines covering the matters stated in the Corporate Governance Code and other corporate governance matters deemed appropriate by the board; such

guidelines shall include or refer to the principles and instruction of the Corporate Governance Code.

- The company shall publish the guidelines and instruction mentioned in the preceding paragraph on its website, if any.
- At each annual shareholders' meeting, the board shall report on the company's governance according to the form prepared by the Ministry of Industry and Commerce and available on its website, which includes the topics listed in Appendix 5 to the Corporate Governance Code, explaining the extent of its compliance with the guidelines and instruction of the Corporate Governance Code, and explaining the reasons for non-compliance, if any.
- The board shall establish a corporate governance committee of at least three independent directors.
- The company shall appoint an employee as the company's corporate governance officer. They shall undertake the tasks of verifying the company's compliance with the corporate governance rules, laws, regulations and decisions issued to implement them. They shall co-ordinate with the corporate governance committee in relation to all corporate governance matters, follow up and co-ordinate with the concerned department on the corporate governance matters.

6.3 Companies Registry Filings

Joint stock companies are required annually to prepare a detailed list approved by the chairman and the managing director, if any, of the names and capacity of the chairman and members of the board, and the managers of the company. The company shall keep a copy of this list and the original shall be sent to the Ministry of Industry and Commerce accompanied by the annual report prepared by the board of directors, the

company's balance sheet and the profit and loss account.

The board of directors of a public shareholding company is required to publish the balance sheet, the profit and loss account, an executive summary of the annual report and the full text of the auditor's report in a local daily newspaper published in Arabic, at least 15 days before the general meeting. Failure to publish the same gives rise to liability that may extend to personal liability, and will render the invitation invalid, and the general meeting voidable.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The board of a joint stock company is required to ensure the integrity of the financial statements submitted to shareholders through appointment of external auditors.

The general assembly meeting of joint stock companies shall appoint one or more auditors for the company and determine their fees upon the proposal of the board of directors. The auditor shall, among others, do the following:

- monitor the company's business;
- give opinion on the validity of the company's financial statements and request to adjust them if there is any impact on their validity; and
- verify the company's ownership of assets and legality of obligations.

Most importantly, the auditor attends the general assembly meetings, reads their report to the shareholders and answers their questions and queries regarding the financial statements for the year end.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The board of a joint stock company shall have rigorous controls for financial audit and reporting, internal control and compliance with law. This is achieved through establishment of an audit committee and development of a whistle-blowing programme.

The board of directors shall form an audit committee consisting of at least three directors, the majority of whom shall be independent, and the chairman of the committee shall be an independent director.

The board of directors shall establish a whistle-blowing programme that will allow the company's employees to report internally their concerns about any improper or suspicious practices in financial reports, internal control systems or any other matters, and make appropriate arrangements for an independent and fair investigation of such practices, while ensuring the confidentiality of such reporting in order to protect them against any adverse reaction or damage that may result from the reporting of such practices.

BURKINA FASO



Law and Practice

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SCP Yanogo Bobson is a law firm specialising in business law and located in Ouagadougou, Burkina Faso in West Africa. Leveraging the expertise of its attorneys, and with nearly thirty years of experience, the firm is able to serve a diverse clientele ranging from start-ups to state-owned enterprises. SCP Yanogo Bobson provides clients with comprehensive consultation services tailored to their needs. The firm places emphasis on corporate and business law matters, particularly mergers, acquisitions and fi-

nancing operations. The lawyers have been recognised for the quality of legal services they provide to both domestic and foreign investors, guiding clients through complex legal landscapes. Comprising a team of fifteen dedicated and qualified individuals, its legal professionals are keen to understand complex legal issues and provide clients with sound and reliable legal advice. SCP Yanogo Bobson is well-equipped to assist both foreign and domestic investors in fully leveraging the Burkinabé economy.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The forms of company governed by the OHADA Uniform Act on the Law of Commercial Companies and Economic Interest Groups (AUDSCGIE) are:

- limited liability companies (Article 309 and following of AUDSCGIE);
- public limited companies (Article 385 and following of AUDSCGIE);
- simplified joint stock company (*société par actions simplifiées*) (Article 853-1 et seq. AUDSCGIE);
- general partnership (*société en nom collectif*) (Article 270 and following of AUDSCGIE);
- economic interest grouping (*groupement d'intérêt économique*) (Article 869 et seq. AUDSCGIE);
- limited partnership (Article 293 and following of AUDSCGIE);
- branches (Article 116 and following of AUDSCGIE); and
- representative or liaison offices (Article 120-1 and following of AUDSCGIE).

1.2 Sources of Corporate Governance Requirements

The main source of corporate governance requirements for companies in Burkina Faso is the OHADA Uniform Act on Commercial Companies and Economic Interest Groups.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies whose shares are listed on the stock exchange must:

- be a public limited company (*société anonyme*) with a board of directors (Article 828 AUDSCGIE);
- have an audit committee (Article 829-1 AUDSCGIE);
- publish annual financial statements (balance sheet, profit and loss account, statement of source and application of funds and annexed statement) (Article 847 AUDSCGIE);
- at the end of the first half of the year, publish an activity and results table and a half-yearly activity report, accompanied by a certificate from the statutory auditor;
- keep a register of registered shares (Article 746-1-2 AUDSCGIE); and
- hold annual general meetings.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Corporate governance is an evolving subject in Burkina Faso, with a growing interest in improving corporate governance practices to enhance transparency, accountability and corporate performance. Thus, the main current issues in corporate governance in our jurisdiction are financial transparency, business ethics and the fight against corruption, training and awareness-raising in corporate governance and ultimate beneficial owner declarations.

2.2 ESG Considerations

The main issues and requirements for companies in terms of information on environmental, social and governance (ESG) issues may be influenced by national regulations and the expectations of local stakeholders. Here are some of the key questions and requirements.

- Regulatory compliance – companies must comply with national ESG regulations, which

may include specific disclosure requirements for certain high-risk sectors or industries. This may involve publishing annual ESG performance reports or participating in voluntary reporting initiatives.

- Environmental risk management – companies are required to identify, assess and manage the environmental risks associated with their activities. This may include, energy, pollution water, earth, ground and air.
- Social and community impact – companies must take into account the social impact of their activities on local communities. This may include the creation of local jobs, respect for human rights, consultation with communities affected by their operations and local content in the mining sector. There is also a draft law on local content in all sectors.
- Corporate governance – companies are required to comply with corporate governance and transparency standards. This may include putting in place disclosure of executive remuneration and registries of ultimate beneficial owners.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal management bodies of a company depend on the type of company. Essentially, these are the general meeting of shareholders, the board of directors, the general management with the general manager, and the deputy general manager.

3.2 Decisions Made by Particular Bodies

The types of decisions of each body are as follows.

Board of Directors

The board of directors determines the direction of the company's business and ensures that it is implemented. It generally takes decisions relating to strategic planning, financial management, risk management, approval of regulatory and loan agreements, and approval of the financial statements.

General Management

The general management team, which, depending on the type of company, comprises the managing director(s), the general manager or chief executive officer and is responsible for the day-to-day running and management of the company. They generally take decisions relating to operational planning, budgeting and the implementation of the strategic objectives of the board of directors.

Shareholders' Meeting

Shareholders are the owners of the company and have the right to vote on major decisions, such as mergers and acquisitions, executive appointments, changes to the company's bylaws, and other significant matters.

3.3 Decision-Making Processes

Shareholders make their decisions at annual or extraordinary general meetings. Subject to the rules specific to each type of company under the provisions of the AUDSCGIE, certain companies, such as limited liability companies, may provide for written shareholders' consultations.

The board of directors takes its decisions at meetings called by the chairman of the board.

General management acts through deeds, contracts, notices, memos and supervises operational teams.

4. Directors and Officers

4.1 Board Structure

Structure of Boards of Directors

A public limited company (*société anonyme*) with a board of directors is managed by a chairman and chief executive officer. In this management mode, two different people hold the two posts. Also, the company can be managed by a chairman of the board and a chief executive officer. In this case, the same person holds the two posts. Indeed, a public limited company with a board of directors is managed in two ways.

The first is management by a chairman and chief executive officer. They chair the board of directors and are responsible for the general management of the company.

The second is the institution of a chairman of the board and a chief executive officer, where the functions of chairman of the board and chief executive officer are exercised by two different persons.

Within the board, specialised committees may be set up to examine specific issues. In short, the board of directors is made up of directors headed by a chairman of the board of directors who may also hold the post of chief executive officer.

4.2 Roles of Board Members

The board of directors plays a crucial role in corporate governance. Here are some of its main roles.

- Strategic management – the board is responsible for defining the company's strategic direction, ensuring that it is in the long-term interests of the company and its shareholders.

- Appointment and supervision of senior management – the board of directors appoints and supervises the company's senior executives, such as the chairman and chief executive officer (CEO) or the managing director (MD). It regularly assesses their performance and may decide to retain or dismiss them.
- Supervision and control – the board supervises the management of the company by its executives, ensuring that it complies with the law, the articles of association and the objectives set. In particular, it can appoint and dismiss directors and monitor their management.
- Fiduciary responsibility – directors owe a duty of loyalty to the company and its shareholders. They must act in the company's corporate interests, avoiding any conflicts of interest and taking decisions in the collective interests of the shareholders.
- Financial reporting – the board is responsible for approving the company's annual financial statements and for communicating this information to shareholders and the regulatory authorities.
- Communication with shareholders – the board communicates regularly with shareholders, in particular by organising the annual general meeting and providing them with transparent information on the company's performance.
- Risk management – the board assesses and manages the risks to which the company is exposed.
- Representation of the company – represents the company in its dealings with third parties, including business partners, regulatory authorities and financial institutions.

4.3 Board Composition Requirements/Recommendations

Under the terms of Article 416 of the AUDSCGIE, a public limited company (*société anonyme*) with a board of directors is made up of at least three and no more than twelve members, whether shareholders or not, or employees or not. It follows from this provision that the board of directors must comprise a minimum of three and a maximum of twelve members.

However, in the event of a public offering, the maximum number of members is increased to 15 and, in the event of a merger, the maximum is increased to the total number of directors in office for more than six months, without exceeding 24.

In addition, the board of directors may also be composed of independent directors, for example members who have no personal or professional ties with the company or its management, in order to ensure objective supervision.

4.4 Appointment and Removal of Directors/Officers

Choice of Directors of a Company

The first directors are appointed by the shareholders in the minutes. During the life of the company, the directors are appointed by the ordinary general meeting. In the event of a merger, the extraordinary general meeting may appoint new directors.

Dismissal of Directors of a Company

According to Article 433 of the AUDSCGIE, directors may be dismissed at any time by the ordinary general meeting, which means that directors may be dismissed *ad nutum*, at their own discretion, without reason, notice or compensation.

Restrictions on the Choice of Directors of a Company

Anyone can be appointed as a director, whether they are a natural person or a legal entity, a shareholder or not, employed or not. However, there are restrictions on who can be appointed as a director. The main restrictions are as follows.

- Incompatibilities – certain persons may be incompatible with the office of director due to their status or activities. For example, persons convicted of certain criminal offences may be prohibited from sitting on the board of directors.
- Term limits – there are limits on the number of terms a person may hold as a director. Thus, under Article 425 of the AUDSCGIE, a person may not simultaneously be a member of more than five boards of directors of public limited companies having their registered office in the territory of a contracting state.
- The legal entities must appoint a permanent representative who is a natural person.
- As far as the employee is concerned, the requirement in this case is that his or her employment contract must correspond to actual employment.

4.5 Rules/Requirements Concerning Independence of Directors

The AUDSCGIE does not provide for specific rules and requirements on the independence of directors. Although the independence of directors is not mandatory under OHADA law, it is often recommended that boards of directors include a certain number of independent directors to strengthen corporate governance. These directors can bring an objective and impartial perspective to board decisions and act as a counterweight to in-house directors.

Such contracts are referred to in the AUDSCGIE, as regulated agreements. These are agreement between the company and one of its directors, managing directors or deputy managing directors, agreements between the company and a shareholder holding 10% or more of the company's capital, any agreement in which a director, managing director, deputy managing director or shareholder holding 10% of the company's capital is indirectly interested or in which they deal with the company through an intermediary. These agreements are subject to prior authorisation by the board of directors.

The authorisation must be sought by the director concerned, who must inform the board as soon as they become aware of such an agreement. Failing this, the agreement is null and void, and it is up to the company's governing bodies or any shareholder to bring an action for nullity. When the board grants its authorisation, it must notify the corporate auditor for approval of the authorised regulated agreement within one month of concluding the agreement to enable the auditor to draw up the special report that must be submitted to the annual general meeting.

4.6 Legal Duties of Directors/Officers

The Principal Legal Duties of Directors and Officers of a Company

The directors and officers of a company have various legal obligations to the company, to shareholders and sometimes even to other stakeholders. Here are some of the main legal obligations.

- Duty of care and loyalty – directors and officers must act prudently and diligently in the performance of their duties. This means that they must make informed and reasonable decisions in the best interests of the company and its shareholders, avoiding conflicts of

interest and acting loyally towards the company.

- Compliance with laws and articles of association – directors and officers must comply with all applicable laws and regulations and with the company's articles of association. This includes compliance with accounting, tax, environmental, labour and other regulations applicable to the company's business.
- Duty of confidentiality – directors and officers are required to maintain the confidentiality of sensitive and privileged information relating to the company, unless such information is legally disclosed or is necessary for the performance of their duties.
- An obligation not to distribute fictitious dividends.
- A prohibition on the publication of false annual summary financial statements.
- A prohibition on the misuse of company assets and/or credit.

4.7 Responsibility/Accountability of Directors

Directors owe their duties to the company and to all the laws and regulations applicable to companies, in particular the AUDSCGIE.

Directors must act solely in the interests of the company.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Holders of Directors' Liability Claims

In event of breach of their duties, directors may be held civilly and criminally liable. In terms of civil liability, a distinction is made between an individual action brought by a shareholder against a director to compensate for damage caused to the shareholder as a result of misconduct or mismanagement in the performance of

his or her duties. This action is brought by the shareholder or the injured party.

There is also the shareholder's action, which seeks to compensate the company for the damage it has suffered. This action is brought either by the management, a group of shareholders or an individual shareholder acting on behalf of the company.

The Consequences of a Breach

If they fail to meet their obligations, directors may be held civilly and criminally liable.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other bases for claims or enforcement against directors or officers may be based on offences such as:

- misuse of corporate assets;
- distribution of fictitious dividends; and
- the publication of false annual summary financial statements.

The Impossibility of Limiting Directors' Liability

Article 168 of AUDSCGle, provides for the nullity of any clause in the company's articles of association limiting the right of action against directors. Also, Article 169 provides for the nullity of any decision by a corporate body to cover the potential liability of a director or officer. It therefore follows from these provisions that the liability of a director or officer cannot be limited. However, the statute of limitation is three years from the date of the harmful event or its disclosure if it was concealed. Also, the limitation period is ten years for crimes.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Directors' Remuneration

In accordance with the provisions of Article 431 of AUDSCGle, directors receive only remuneration for their duties and are not entitled to any other remuneration. Only the ordinary general meeting may decide to grant director's fees and the board of directors has the sole responsibility for allocating them which may be shared equally and unequally between its members.

In addition to their fees, directors may receive exceptional remuneration for assignments entrusted to them. The decision to grant exceptional remuneration is taken by the board of directors. However, they give rise to a special report by the auditor to the shareholder's annual general meeting.

The Consequences for Failing to Comply With These Approval Requirements

In the event of failure to comply with the requirements for the remuneration of directors, directors will not be entitled to any remuneration.

4.11 Disclosure of Payments to Directors/Officers

Public (or Other) Disclosures

The AUDSCGle, does not specifically address the disclosure of remuneration, fees or benefits granted to directors and officers, but it does establish a general framework for transparency and corporate governance. In this context, public limited companies (*société anonyme*) are generally required to publish an annual report providing detailed information on the management of the company, including the remuneration of directors and officers. This report may include the specific amounts of remuneration, the types of remuneration (salaries, bonuses, benefits in

kind, etc) and the company's remuneration policies. Directors' remuneration is the subject of a report by the statutory auditor, which is presented to the general meeting of shareholders.

They are also required to disclose directors' and officers' remuneration in the annual financial reports filed with the relevant regulatory authorities.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Between the shareholders and the company, there is a relationship of collaboration, information and control for the good management of the company. This relationship requires loyalty and transparency, and is essentially governed by the provisions of the AUDSCGIE.

5.2 Role of Shareholders in Company Management

The shareholders have a key role in decision-making and supervision of the company's management, and in approving certain aspects of the company's life, such as financial statements, regulated agreements and profit distribution. The shareholders have rights and obligations. They have the right to vote on the company's strategic decisions and are entitled to dividends.

Although shareholders are not involved in the company's daily management, they do have the power to influence the company's strategic decisions by holding management to account and approving major decisions that are in the company's best interests.

5.3 Shareholder Meetings

For each type of company governed by the AUDSCGIE, there is an obligation to hold an annual general meeting six months after the close of each financial year which is 31 December. In addition, by law certain decisions, such as a change of registered office or an increase in share capital, must be taken at an extraordinary general meeting.

The rules governing the holding of general meetings are as follows.

- Convening meetings – the AUDSCGIE, Law stipulates a minimum notice period of fifteen days for convening shareholders' meetings, unless shareholders waive the notice period. The notice of meeting must include identification of the company, the day, place and time of the meeting, the agenda and the nature of the meeting (ordinary, extraordinary or special).
- Right of disclosure – at an ordinary shareholders' meeting, shareholders are entitled to disclosure of summary financial statements, statutory auditors' reports, management reports by the manager or the board of directors, and so on.
- Compliance with quorum requirements, depending on the type of decisions to be taken – for a simple majority (fifty plus one), a qualified majority (two-thirds) unless a higher majority is provided for in the company's articles of association.
- Indication in the minutes of the meeting of the date and place of the meeting, the full names of the shareholders present, the documents submitted for discussion, the text of the resolutions, a summary of the discussions, the text of the resolutions put to the vote and the results of the votes (Article 134 of the AUDSCGIE).

5.4 Shareholder Claims

The main claims of shareholders against company or directors are as set out below:

- Unequal distribution of dividends – If shareholders consider that the company is distributing dividends in unfair or discriminatory ways, they can contest this practice in court. Article 889 of the AUDSCGle, stipulates that company directors who, in the absence of an inventory or by means of a fraudulent inventory, knowingly distribute fictitious dividends among shareholders or associates are liable to criminal penalties.
- Decisions prejudicial to shareholders' interests – Shareholders may take legal action against the company or its directors if the latter make decisions prejudicial to shareholders' legitimate interests.
- Violation of the company's articles of association – Shareholders may contest any action taken by the company or its directors which contravenes the provisions of the company's articles of association.
- Failure by directors to meet their obligations – Shareholders can remove directors from office if they fail to meet their obligations, and sue them if their actions cause them prejudice.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Obligation of Information for Publicly Traded Companies

With regard to disclosure requirements, the provisions of Article 86 and following of the AUDSCGle, provide that companies offering shares to the public must publish a public information document in the country of the company's registered office and, where applicable, in the other countries in which the public is solicited. This document contains the information necessary

to enable investors to make an informed evaluation of the assets and liabilities, financial position, results and prospects of the issuer and any guarantors, as well as the rights attached to the shares.

The information document must be distributed by:

- publication in newspapers authorised to carry legal announcements;
- making a brochure available for consultation by any person at the company's registered office and at institutions responsible for the financial servicing of the negotiable shares;
- posted on the company's website or, where applicable, on the websites of financial intermediaries placing or selling the negotiable securities;
- posted on the website of the stock exchange where admission to trading is requested; and
- placed online on the website of the competent authority of the country of the registered office if the latter has decided to offer this service.

Disclosure Obligations in Relation to the Ultimate Beneficial Owner of Publicly Traded Companies

Pursuant to Decree no 2022-0234/PRES-TRANS/PM/MATDS/MJDHRI/MEFP on the obligation to declare and keep a register of the ultimate beneficial owners of legal entities and legal entities, any company, whether or not it is quoted on the stock exchange, must declare its ultimate beneficial owners to the commercial court and keep a register of ultimate beneficial owners endorsed and initialled by said court.

The 2022 and 2023 finance acts amending the General Tax Code (CGI) of Burkina Faso introduced a new system of beneficial ownership

declaration, requiring legal entities of all forms and activities to identify their ultimate beneficial owners, and to keep a register of ultimate beneficial owners at their registered office.

The declaration of ultimate beneficial owners is drawn up using a form that conforms to the administration's standard form. It should be noted that the form used by the tax authorities is different from that used by the commercial court. Information on the stock market of listed companies must be specified.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

In a public limited company (*société anonyme*), simplified joint stock companies (*sociétés par actions simplifiées*) and, where applicable, in limited liability companies (*sociétés à responsabilité limitée*), the annual summary financial statements and the management report are sent to the statutory auditors at least 45 days before the date of the ordinary general meeting in accordance with Article 140 of AUDSCGIE.

Article 269 of the AUDSCGIE, also requires commercial companies to file with the Trade and Personal Property Credit Register, within one month of their approval by the competent body, the summary financial statements – ie, the balance sheet, the income statement, the financial table of resources and uses, and the appended statement for the past financial year.

Article 95 of the General Tax Code states that companies are required to declare, by 30 April each year at the latest, the amount of their taxable income for the financial year ended 31

December of the previous year using a form that complies with the tax authorities' model.

6.2 Disclosure of Corporate Governance Arrangements

Companies must disclose the following corporate governance arrangements:

- regulated agreements (between a public limited company and one of its directors, managing directors or deputy managing directors);
- agreement between a company and a shareholder holding 10% or more of the company's capital;
- agreements between a company and a business or legal entity, if one of the directors, managing director or deputy managing director or a shareholder holding 10% or more of the company's capital is the owner of the business or a partner with unlimited liability, manager, managing director or deputy managing director, managing director or deputy managing director or other corporate officer of the contracting legal entity (Article 438 et seq. AUDSCGIE) are presented to the statutory auditors and shareholders;
- sureties, endorsements and guarantees (Article 449 AUDSCGIE); and
- prohibited agreements (Article 4450 AUDSCGIE).

6.3 Companies Registry Filings

Companies are required to make the following filings with the companies' registry in Burkina Faso:

- acts performed at the time of incorporation;
- acts amending the Trade and Personal Property Credit Register (RCCM);
- securities (Article 747 AUDSCGIE); and
- the register of ultimate beneficial owners.

The companies' registry is in principle publicly available but accessing the information may be more difficult in practice as the registries are not all fully computerised.

The consequences of failing to make these declarations are that they cannot be invoked against third parties.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

In simplified joint stock companies (*sociétés par actions simplifiées*) and in limited liability companies (*sociétés à responsabilité limitée*), the appointment of a statutory auditor is only compulsory under certain conditions. However, it is compulsory for public limited companies.

The statutory auditor is independent of the company, although appointed by the shareholders. He or she certifies the company's financial statements (Article 710 et seq. AUDSCGIE) and is liable for them.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

There are requirements for directors in connection with the management of risk and internal controls in the company. Indeed, pursuant to legal provisions, the board of directors must:

- determine the direction of the company's business and oversees its implementation;
- carry out any checks and verifications it deems appropriate; and
- provide each director with all the documents and information required to perform his or her duties (Article 435 of AUDSCGIE).

CABO VERDE



Law and Practice

Contributed by:

Nelson Raposo Bernardo, Joana Andrade Correia,
Júlio Martins Júnior and Manuel Esteves Albuquerque

Raposo Bernardo & Associados

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Raposo Bernardo & Associados is dedicated to turning governance challenges into business opportunities. Key services focusing on governance are as follows: ESG strategy development – crafting tailored governance strategies that align with client business goals, identifying and prioritising key governance issues relevant to the industry, and integrating ESG considerations into overall business strategy; governance policy and compliance – advising on the development and enforcement of good governance policies, and ensuring compliance with local and international governance regulations; stakeholder engagement and communica-

tion – facilitating effective communication with stakeholders on governance matters, helping clients build and maintain a positive reputation, and advising on transparency and disclosure practices; sustainability reporting and impact assessment – assisting with the preparation of sustainability reports in accordance with global standards (eg, GRI and SASB), conducting environmental and social impact assessments, and providing metrics and analytics to measure governance performance. The firm has been assisting in navigating regulatory frameworks and compliance to improve companies' governance ratings.

Authors



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RAPOSO BERNARDO

1. Introductory

1.1 Forms of Corporate/Business Organisations

In Cabo Verde, most business organisations are incorporated in the form of companies with distinct legal personality. The corporate forms are as follows.

Public Limited Companies (Sociedade Anónima or SA) – Used for Large Companies

This type of company has the following characteristics.

- Minimum share capital of EUR0.01.
- A minimum of two shareholders. A single-shareholder public limited company incorporation is permitted if the single shareholder is another company.
- As a general rule, public limited companies are incorporated by means of a private document (articles of association). Additional formalities may apply if the shareholders perform contributions in kind.
- As a rule, the transfer of shares is free and may be carried out by means of an agreement between the parties.

The governing bodies of a public limited company are as follows.

- (a) A management board, generally with a minimum of three members. Management can be entrusted to one director if the turnover for two consecutive years is expected to be less than CVE10 million. In addition to the election of the effective members of the board of directors, substitute directors must be elected in numbers not exceeding one third of the effective directors – this means three effective members and one substitute

member, or one effective member and one substitute.

- (b) A shareholders' meeting.
- (c) A supervisory board (three members) or one auditor – a member of the supervisory board or the auditor must be certified.
- (d) An auditor (for large companies).
- Shareholders' liability is limited to capital subscribed, but shareholders are jointly and severally liable for all contributions contained in the by-laws.
- Flexibility of capital – only registered shares are allowed. Registered shares are transferred by endorsing the share certificate in the name of the transferee. Notice must be given to the company for the purposes of registration in the share book. Book-entry shares are transferred by registration in the transferee's bank account. The only limit on the free transfer of shares may arise from any pre-emption rights that have been established by the shareholders in the articles of association.

Limited Liability Partnership (Sociedade por Quotas) – Primarily Used for Small Businesses

This type of company has the following characteristics.

- A minimum share capital of EUR0.01.
- A minimum of two shareholders as a rule. Single-shareholder limited liability company incorporation is permitted.
- As a general rule, limited companies are incorporated by means of a private document (articles of association). Additional formalities may apply if the shareholders perform contributions in kind.
- The transfer of shares may be carried out by means of an agreement between the parties, except when the incorporation has been made through public deed.

- The company is governed by management with one or more directors. An auditor is not mandatory, but companies that do not have a supervisory body must appoint a certified auditor to carry out the statutory audit if turnover is greater than CVE10 million and/or the number of employees is more than ten.
- Shareholders' liability is limited to capital subscribed, but shareholders are jointly and severally liable for all contributions contained in the by-laws.
- The transfer of shares must be made by written agreement between the parties. The articles of association may set limits or conditions on the transfer of shares or pre-emptive rights in favour of other shareholders or the company itself.

1.2 Sources of Corporate Governance Requirements

Corporate governance requirements are derived from laws and regulations, recommendations and internal rules set forth by companies themselves.

Laws and Regulations

These contain the majority of corporate governance rules and requirements:

- The Commercial Companies Code (CSC) approved by Legislative Decree No 2/2019.
- The Securities Code in its latest version approved by Law 101/IX/2020.
- The Banking Law approved by Law No 62/VIII/2014.

Recommendations

Listed companies and the ones operating in banking and financial sector are subject to additional recommendations issued by corporate governance codes, to which they must refer.

They must also take into consideration recommendations issued by the by sectoral regulatory entities, such as the Central Bank of Cape Verde or the Multisectoral Economic Regulatory Agency.

Internal Rules

Companies may adopt internal rules, such as by-laws, board internal regulations, codes of ethics or of conduct which set forth specific corporate governance rules and requirements.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Listed companies are subject to mandatory corporate governance requirements and recommendations. First of all, only companies organised as Public Limited Companies (*Sociedade Anónima* or SA) are authorised to trade their shares on a regulated market.

To promote a high corporate governance standard, the Securities Code contains corporate governance standards, especially with regard to compliance with the duty of information. Companies must produce annual information on corporate governance, in the following terms.

- Capital structure, including indication of shares not admitted to trading, different categories of shares, rights and duties inherent to them and percentage of capital that each category represents.
- Possible restrictions on the transferability of shares, such as consent clauses for sale, or limitations on share ownership.
- Qualified holdings in the company's share capital.
- Identification of shareholders holding special rights and description of these rights.

- Control mechanisms provided for in a possible system of employee participation in capital, to the extent that voting rights are not exercised directly by them.
- Possible restrictions on voting rights, such as limitations on the exercise of voting depending on the ownership of a number or percentage of shares, deadlines imposed for the exercise of voting rights or systems for highlighting rights with patrimonial content.
- Shareholder agreements that are known to the company and may lead to restrictions on the transfer of securities or voting rights.
- Rules applicable to the appointment and replacement of members of the management body and amendments to the company's statutes.
- Powers of the management body, particularly with regard to decisions to increase capital.
- Significant agreements to which the company is a party and which come into force, are amended or terminate in the event of a change in control of the company following a public takeover bid, as well as the respective effects, unless, by their nature, their disclosure would be seriously detrimental to the company, unless the company is specifically obliged to disclose such information due to other legal imperatives.
- Agreements between the company and the members of the management body or employees that provide for compensation in the event of the employee's resignation, unfair dismissal or termination of the employment relationship following a public takeover bid.
- Internal control and management risk systems implemented in the company.

The following mandatory corporate governance mechanisms are also envisaged in these companies.

- The existence of the Certified Auditor as an autonomous body, not being part of the Supervisory Board.
- The Supervisory Board must include at least one member who has a higher education degree appropriate to the exercise of their functions and knowledge in auditing or accounting and that is independent.
- The Supervisory Board must be composed of a majority of independent members.

The members of the board of general meeting:

- are subject to the incompatibility regime;
- must be independent;
- can only be removed by the general assembly with just cause; and
- can only receive fixed remuneration.

As for the members of the management body, a regime prohibiting the waiver of deposits to hold administrators liable is established.

The Conduct Code (Circular 3/2012), issued by the Cape Verdean stock exchange, lays down further rules on the corporate governance of listed companies.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

As has occurred in several jurisdictions, the factors underpinning ESG are increasingly being introduced into the reality of companies in Cabo Verde.

The legislative changes resulting from the approval of the new Commercial Companies Code also reinforced the corporate rights of minority shareholders, as well as access to company information.

Contributed by: Nelson Raposo Bernardo, Joana Andrade Correia, Júlio Martins Júnior and Manuel Esteves Albuquerque, **Raposo Bernardo & Associados**

Furthermore, several companies are creating internal Corporate Governance regulations based on internationally consolidated principles.

2.2 ESG Considerations

There are no mandatory requirements for companies in relation to reporting on ESG issues. However, there are certain recent developments on corporate governance that might impact ESG issues, such as the creation of the Institute for Corporate Governance, a private entity aiming to work and develop the matter in Cabo Verde.

It must also be noted that the launch of some financial products, called social, green and blue bonds, aim to allow the financing of sustainable projects within the framework of ESG policies.

Some entities operating in regulated sectors, such as telecommunications, energy, banking and finance, include information on ESG in their reports.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

Principal bodies of Public Limited Companies (*Sociedade Anónima*, or SA) are as follows.

- Management Board – generally, there is a minimum of three members. Management can be entrusted to one director if the turnover for two consecutive years is expected to be less than CVE10 million. In addition to the election of the effective members of the board of directors, substitute directors must be elected in numbers not exceeding one-third of the effective directors – this means three effective members and one substitute

member, or one effective member and one substitute.

- Supervisory Board – composed of three members or one auditor – a member of the supervisory board or the auditor must be certified.
- Shareholders' Meeting – the board of the general assembly is composed of a President and a Secretary.
- Auditor – applicable in case of large companies and listed companies.

Principal bodies of Limited Companies (*Sociedade Por Quotas*) are as follows.

- Management board – the company is governed by management with one or more directors.
- Shareholders' meeting – the board of the general assembly is composed of a President and a Secretary.
- Supervisory board.
- An auditor is not mandatory, but companies that do not have a supervisory body must appoint a certified auditor to carry out the statutory audit if turnover is greater than CVE10 million and/or the number of employees is more than ten.

3.2 Decisions Made by Particular Bodies

The powers and types of decisions made by the corporate bodies differ depending on the corporate form of the company.

Sociedade Anónima

The board of directors is competent to determine the strategic orientations of the company's business and ensure their implementation within the limits of the company's interest. The board of directors is responsible for managing the activities of company, and must be subordinated to the deliberations of the general meeting or inter-

ventions of the supervisory board only in cases where the law or company articles so determine. In particular, the board of directors:

- chooses its president, except when the company's articles of association attribute this responsibility to the shareholders;
- requests to convene general meetings;
- prepare and submit the annual reports and accounts to be submitted for shareholder approval;
- acquisition, disposal and encumbrance of real estate;
- provision of personal or real guarantees and deposits by the company;
- opening or closing of establishments or important parts thereof;
- important extensions or reductions in the company's activity;
- establishment or termination of lasting and important co-operation with other companies;
- change of headquarters and capital increases, under the terms set out in the articles of association;
- merger, spin-off and company transformation projects; and
- any other matter on which any administrator requires deliberation by the board.

The CEO and the deputy CEOs, if any, are in charge of the day-to-day management of the company, within the limits of the corporate object of the company and the board of directors' powers.

Sociedade por Quotas

In the *Sociedade por Quotas*, the managing directors have the broadest powers to manage the company and represent it to third parties, within the limits of the corporate purpose and shareholders' powers.

Refer to **5.2 Role of Shareholders in Company Management** for a description of the shareholders' decision-making powers.

3.3 Decision-Making Processes

The decisions of the Board of Directors are adopted either following a board meeting (held in-person or via a teleconference), or by having all directors sign a decision.

The Board of Directors (BOD) meets whenever it is called to by the President or by two other administrators. The BOD must meet at least once each month, unless otherwise provided for in the articles of association. The directors must be asked to convene in writing, with adequate advance notice, except when the contract of the company or a board regulation provides for the meeting on pre-fixed dates or another form of call.

The BOD cannot deliberate without being present or represented by the majority of its members. Decisions are taken by majority vote of directors present or represented.

Shareholders' meetings are called by the president or, in the special cases provided for by law, by the supervisory board or by the court, at least 21 days in advance.

The shareholders who, according to the law and the by-laws, are entitled to at least one vote, have the right to be present at the general meeting and discuss and vote at such meeting.

As a rule, the general assembly can make decisions, in the first call, regardless of the number of shareholders present or represented. During second call, the assembly may decide regardless of the number of shareholders present or

represented and the capital represented by them.

So that the general assembly can deliberate in the first call on matters for which the law requires a qualified majority, shareholders holding at least 1/3 of the share capital with voting rights must be present or represented.

The general assembly decides by a majority of votes issued, whatever the percentage of share capital represented therein, unless otherwise provided by law or the contract, and abstentions are not counted.

The decision on changing the articles of association, merger, division, transformation, dissolution of the company or other matters for which the law requires a qualified majority without specifying it, must be approved by 2/3 of the votes cast, whether the assembly meets in the first or second call.

4. Directors and Officers

4.1 Board Structure

In Public Limited Companies (*Sociedade Anónima*), the Board of Directors is made up of at least three members (there must always be an odd number). However, the law allows administration to be entrusted to a single director whose turnover, for two consecutive years, is less than CVE10 million (GBP76,432.69).

If a legal person is appointed director, they must appoint a natural person to hold the position in their own name.

The Board of Directors can further delegate the management and representation powers to one

or more individuals, directors or third parties, or to an executive committee.

In the case of *Sociedade por Quotas*, management is carried out by one or more natural persons (partners or non-partners).

4.2 Roles of Board Members

The Companies Code establishes that the board of directors is a collegiate body. As a principle, the directors collectively exercise the functions assigned to the board and they do not have any individual powers, except for the chairperson of the board. The chairperson is in charge of organising and directing the work of the Board of Directors and reporting to the general meeting.

The Board of Directors may grant specific assignments to individual directors, in order to improve the corporate governance of the company and facilitate the board's mission.

4.3 Board Composition Requirements/ Recommendations

The following composition requirements are in place.

- The Board of Directors of a *Sociedade Anónima* is made up of at least three members (there must always be an odd number).
- The Board of Directors of a *Sociedade por Quotas* is carried out by one or more natural persons (partners or non-partners).
- Directors may be individuals or legal persons. If a legal person is appointed director, they must appoint a natural person to hold the position in their own name.
- Along with the election of effective members of the Board of Directors, directors may be elected as substitutes in a number that does not exceed one third of the effective administrators.

Special Board of Directors composition requirements may also apply to specific types of companies due to the special regime to which they are subject (for example, aviation, banking and finance).

4.4 Appointment and Removal of Directors/Officers

Electing Directors

The members of the BOD are appointed in the by-laws or elected by the general assembly. The directors are appointed or elected for a period set out in the company's articles of association, and in the absence of an appointment period, it is understood that the appointment is made for four calendar years, with re-election being permitted.

The articles of association may stipulate that the election of the Board of Directors must be approved by a certain percentage of capital or that election of some of them must be approved by the majority of votes cast by a certain category of shares, as well as stating that certain categories of shares are granted the right to elect a certain number of directors, in a number not exceeding one third of the total.

The articles of association may establish that, for a number of directors not exceeding one, two or three, depending on whether the total number is three, five or more than five, an isolated election is carried out, between persons proposed on lists subscribed by groups of shareholders, as long as none of these groups has shares representing more than 20% or less than 10% of the total share capital.

Substitute Directors

If a director is definitely missing, he or she must be replaced, as follows.

- By calling substitutes made by the president, according to the order in which they appear on the list submitted to the general meeting of shareholders.
- By co-option, when there are no substitutes, unless there are not enough current directors for the board to function.
- By designating a substitute by the supervisory board, in the event that there has been no co-option within 60 days of the absence.
- By election of a new director.

Removal and Renunciation

Any member of the board of directors may be removed by resolution of the general meeting, at any time.

One or more shareholders holding shares corresponding to at least 10% of the share capital may, until a general meeting has been called to deliberate on the matter, request the judicial dismissal of a director, based on just cause.

In particular, serious breach of the administrator's duties and his/her inability to carry out his/her duties normally constitutes just cause for dismissal.

Any director may resign from the exercise of his/her duties, by means of a written document addressed to the chairperson of the BOD. The resignation only takes effect 30 days after it is communicated, unless, in the meantime, a replacement is designated or elected. Resignation without just cause must be communicated within a reasonable period of time.

4.5 Rules/Requirements Concerning Independence of Directors

The Commercial Companies Code enshrines some legal provisions that aim to highlight the need for markedly independent management of

commercial companies and avoid conflicts of interest.

Firstly, a general prohibition is established on granting loans or any form of credit to its directors, providing guarantees for obligations assumed by them or providing them with advances on salaries exceeding one month.

Furthermore, it was established that, unless expressly consented to by the General Assembly, transactions are concluded between:

- the company and the director, in their own name, directly or through an intermediary; or
- the company and the director, representing a third party;

and the company is one in which a director performs management functions.

These prohibitions remain in place in the year following the termination of duties by the director and are extended to transactions concluded with companies that are in a controlling or group relationship with the one in which the contracting party is a director.

Furthermore, the Commercial Companies Code establishes that during the period for which they were appointed or elected, directors cannot exercise, in the company or in companies that are in a controlling or group relationship with them, any temporary or permanent functions at the same time, under an employment or service-provision contract, or regarding entering into any such contracts aimed at providing services when a director's duties cease. When someone who is linked to the company by an employment or service provision contract is appointed or elected as a director, this contract is suspended and

is resumed immediately after the termination of duties.

Unless express authorisation is given at a general meeting, the director cannot carry out, on his/her own or on behalf of others, activities competing with those actually carried out by the company, nor can they carry out functions in a competing company or be appointed on behalf of it.

4.6 Legal Duties of Directors/Officers

Directors stand in a fiduciary relationship towards the company. Directors are expected to act in good faith and in the best interest of the company at all times. This involves preserving the company's assets as well as furthering the company's business interests.

In general, directors must conduct the company's affairs with the due care of a prudent and diligent business-person, in particular in accordance with the applicable laws and the articles of association (duty of legality) and taking into account the interests of shareholders and employees.

The duty to act diligently includes, in particular, the duty to obtain the necessary technical competence and sufficient knowledge of the company's activities, and the duty to act in informed terms, free from any personal interest and in accordance with criteria of business rationality.

The members of the supervisory body must act in accordance with high standards of professional diligence and loyalty.

4.7 Responsibility/Accountability of Directors

The directors owe their duties to the company. They always have to act in the best interests of the company. As established by the law, they

shall act also taking into account, to a certain extent, the interests of the shareholders, creditors and employees of the company.

4.8 Consequences and Enforcement of Breach of Directors' Duties

The Companies Code organises the topic of directors' civil liability into three large groups:

- civil liability towards company (Articles 78 and 79 of the CSC);
- civil liability for social creditors (Article 84 of the CSC); and
- civil liability towards partners and third parties (Article 85 of the CSC).

Civil Responsibility Towards the Company

Article 79, paragraph 1 establishes the principle that the members of the management body are answerable to the company for damages caused to it by breach of legal and contractual duties. A presumption of guilt is attributed to the members of the management body, which may be revoked *"if they prove that they acted without fault"*.

Responsibility is joint among directors.

The operationalisation of the civil liability mechanism of the members of the management body towards the company depends on the deliberation of the shareholders, taken by an absolute majority, and must be proposed within a period of six months counting from said deliberation, and for the exercise of the right of compensation, the partners may appoint special representatives. The civil liability of administrators can even be triggered during the meeting that considers the financial statements, although this matter is not included in the notice.

Civil Liability Towards Creditors

The civil liability of the board of directors towards creditors arises from the culpable non-compliance with legal or contractual provisions intended to protect them, and the social assets become insufficient to satisfy the respective credits.

The protection of corporate creditors is reinforced, as the compensation obligation cannot be excluded by the company's resignation or transaction or by the fact or omission based on a resolution of the general meeting.

Creditors' rights may even be exercised during the insolvency process by the administration of the insolvent estate.

Civil Liability Towards Shareholders and Third Parties

Finally, the Companies Code establishes a civil liability regime for the management body towards partners and third parties for damages directly caused to them in the exercise of their functions. This regime is complemented by the provisions of the Civil Code, which reinforces liability based on breach of contractual and legal duties.

The responsibility of the members of the management body towards shareholders and third parties is joint and several.

It is important to highlight that the civil liability regime for members of the management body also applies to *"other people entrusted with management functions"*. In other words, it does not only apply to members of the management body formally designated by the partners. It applies to directors and managers and not just in formal terms.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In Cabo Verde, directors and officers can be held liable for criminal and civil charges. Regarding criminal liability, in certain circumstances, directors may also be subject to criminal penalties for other violations of the Corporate Law – for example:

- for knowingly making a false or misleading statement to the public;
- for knowingly preparing or approving incorrect or misleading financial statements; or
- for obstructing the conduct of an audit by statutory auditors or auditors appointed for the conduct of an extraordinary audit.

Criminal and/or administrative penalties are provided for by other special laws, particularly in relation to tax, labour, health, safety and environmental violations.

Directors and officers can also be civilly liable if they commit a breach of laws and/or regulations applicable to the company (breach of the articles of association or internal regulations).

Liability cannot be limited and the law requires managers to take out insurance. However, it may be waived by the general meeting, except in companies issuing securities admitted to trading on the stock exchange and in large companies.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The general meeting of shareholders or a committee appointed by it is responsible for setting the remuneration of each director, taking into account the functions performed and the economic situation of the company.

The remuneration may be certain or partially consist of a percentage of the year's profits, but the maximum percentage allocated to directors must be authorised by a clause in the company's articles of association.

4.11 Disclosure of Payments to Directors/Officers

All companies in Cabo Verde are required to disclose the total remuneration of the management board in the annual financial statements.

Directors' fees must also be disclosed to the tax authorities as a form of income.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The entire structure of the company is defined by the shareholders when the company is formed. The purpose of the company is determined by its shareholders in the articles of association. The company and its shareholders are legally bound by the by-laws, which constitute the company's internal regulations. As a result, shareholders collectively own the company.

The shareholders have the right to appoint corporate bodies, to attend and vote at AGMs, to receive dividends, and other rights. They may also, in certain circumstances, be called upon to finance the company.

For private limited companies, the identity of shareholders and their respective capital quotas must be registered at the Commercial Registry. This registration is publicly accessible, and anyone may request a certificate from the registry showing the current shareholders. The situation differs for public limited companies. Sharehold-

ers are registered in a share register (book) that must be kept at the company's head office. However, this register is not public, and there is no legal obligation to update the list of shareholders at the Commercial Registry. The only information that is publicly available through the registry concerns the company's initial shareholders.

5.2 Role of Shareholders in Company Management

One of the basic rules of corporate law under the Companies Code is that the business shall be managed by or under the direction of a board of directors. Thus, shareholders are generally not involved in the direct management of the company.

However, they may have some influence on management, as the law gives shareholders the right and the power to elect the board of directors, as well as the right to vote on and approve extraordinary transactions, such as any amendment to the certificate of incorporation or the by-laws, a merger, consolidation or conversion, the sale of all or a substantial amount of the assets of the corporation or the dissolution.

Shareholders participate in the decision-making process through the exercise of their voting rights in the general meetings.

5.3 Shareholder Meetings

The ordinary shareholder meeting of the company is held regularly once a year, within the first three months following the end of each financial year, to:

- deliberate on the management report and accounts for the year;
- deliberate on the proposed application of results;

- carry out a general assessment of the administration and supervision of the company and, if applicable and although these matters are not on the agenda, proceed with the dismissal of members of the corporate bodies, when the general assembly has the power to do so, or express their distrust of them, when the authority to dismiss them lies with the supervisory board; and
- carry out elections within its competence.

An extraordinary shareholder meeting may be convened on the initiative of the chairperson of the Board of General Meetings, by the Supervisory Board or by the court, whenever deemed necessary, in order to resolve the matters that are reserved for the exclusive competence of the shareholder meeting or any other matter that the BOD may consider of such importance that it requires the approval of the general meeting or at the request of shareholders holding at least 5% of the company's share capital (2% in the case of a listed company), in exercise of the minority rights provided under the Companies Law.

The shareholder meeting is convened 21 full days prior to the date of the meeting through the publication of the invitation, which includes the items of the agenda, details of the place and time of the general meeting and rights that the shareholders may exercise within the 21-day period and during the meeting.

5.4 Shareholder Claims

According to the law, regardless of the claim for compensation for individual damages caused, one or more shareholders who own at least 5% of the share capital may file a liability action against members of the management body, with a view to reparation, in favour of the company,

for the loss it has suffered, when the company has not filed it.

5.5 Disclosure by Shareholders in Publicly Traded Companies

In companies listed on the stock exchange, the law establishes that anyone who reaches or exceeds a shareholding of 10%, 20%, one third, half, two thirds or 90% of the voting rights corresponding to the share capital of a public company, subject to Cape Verdean personal law, and anyone who reduces their participation to a value lower than any of those limits must, within four business days after the day of the occurrence of the fact or its knowledge:

- inform the General Audit of the Securities Market and the company of this fact; and
- make the entities referred to in this section aware of the situations that determine the attribution to the participant of voting rights inherent in securities belonging to third parties.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Companies are required to file various documents relating to their accounts for the previous financial year with the registrar of commercial companies.

The filing covers the following documents:

- the annual accounts;
- the management report;
- minutes of approval of the accounts for the year and application of results;
- balance sheet, income statement and annex to the balance sheet and income statement;

- legal certification of accounts; and
- opinion of the supervisory body, if such body exists.

The management report is prepared by the directors and covers principally the company's corporate governance arrangements, the performance of the company during the year under review, and the outlook for the coming year.

6.2 Disclosure of Corporate Governance Arrangements

Corporate governance arrangements are disclosed as part of the regulatory reports expected from companies.

6.3 Companies Registry Filings

In Cabo Verde, the body responsible for company incorporation and registration is the Commercial Registry Services, under the supervision of the Directorate-General of Registries, Notary and Identification (*Direção-Geral dos Registos, Notariado e Identificação*), which is part of the Ministry of Justice.

The Commercial Registry does not act as a regulatory or supervisory authority in the corporate governance sense. However, it exercises administrative control over the legality and formal regularity of the documents submitted for registration. Notably, the registry does not supervise the conduct of directors, shareholders, or internal affairs of companies, nor does it intervene in disputes unless by judicial order.

Any updates to the constitutive documents during the life of the company must be filed with the companies registry. These updates and their related corporate documents are publicly available and include amendments to the articles of association, changes to board composition,

transfers of the registered office, and changes to the share capital, among others aspects.

In the event of failure to comply with the filing obligations, companies or their officers may be exposed to administrative fines.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The appointment of an external auditor by the shareholders' ordinary general meeting becomes mandatory if, at the end of the financial year, the company exceeds at least one of the following thresholds:

- turnover exceeding CVE200 million (over GBP1.528 million); and
- total net assets exceeding CVE15 million (GBP114,654.19).

Auditors are subject to certain requirements regarding their independence, which prohibits them from having any personal, financial or professional relationships that are incompatible with the functions of an auditor.

Companies issuing securities admitted to trading on the stock exchange are also required to have an external auditor.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The law establishes that members of the company's management bodies must act with diligence and loyalty, in the interests of society, having taken into account the interests of partners and employees. The duty to act diligently includes, in particular, obtaining the necessary technical capacity and sufficient knowledge of the company's activities.

Therefore, such a duty must be understood as also including the obligation of the company's management to establish risk management policies and internal control systems in the more general context of promoting the company's interests and business activity.

Trends and Developments

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Raposo Bernardo & Associados is dedicated to turning governance challenges into business opportunities. Key services focusing on governance are as follows: ESG strategy development – crafting tailored governance strategies that align with client business goals, identifying and prioritising key governance issues relevant to the industry, and integrating ESG considerations into overall business strategy; governance policy and compliance – advising on the development and enforcement of good governance policies, and ensuring compliance with local and international governance regulations; stakeholder engagement and communica-

tion – facilitating effective communication with stakeholders on governance matters, helping clients build and maintain a positive reputation, and advising on transparency and disclosure practices; sustainability reporting and impact assessment – assisting with the preparation of sustainability reports in accordance with global standards (eg, GRI and SASB), conducting environmental and social impact assessments, and providing metrics and analytics to measure governance performance. The firm has been assisting in navigating regulatory frameworks and compliance to improve companies' governance ratings.

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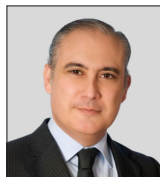
CABO VERDE TRENDS AND DEVELOPMENTS

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Conflicts of Interest and Duty of Loyalty in Corporate Governance: The Current Regime in Cape Verde's Commercial Companies Code

One of the principal novelties introduced by the new Cape Verde Commercial Companies Code pertains to the subjects of conflict of interest and the duty of loyalty within the framework of a business organisation. Contemporary corporate governance increasingly necessitates mechanisms that assure not only the formal legality of corporate resolutions but also their substantive legitimacy. Furthermore, a significant challenge for commercial companies lies in the prevention and management of conflicts of interest arising between the holders of corporate offices and the company itself.

Within emerging economies such as Cape Verde, these subjects have been acquiring increasing prominence to the extent that they facilitate the generation of trust, the professionalisation of management, the attraction of investors, and the securing of sustainable development for the local business structure. In this context, the Cape Verde Commercial Companies Code (CSCV) adopts a comprehensive set of regulations aimed at guaranteeing the duty of loyalty of administrators and the safeguarding of the integrity of the corporate decision-making process. The present article endeavours to analyse the legal regime governing conflicts of interest and the duty of loyalty owed by administrators, as viewed through the lens of the CSCV, exploring their ethical, legal, and fiduciary dimensions, and contextualising Cape Verde's approach in relation to prevailing international best practices.

The implementation of an efficacious corporate governance framework yields a multitude of benefits for enterprises operating within Cape Verde, thereby contributing significantly to the

nation's sustainable economic growth. A robust governance structure enhances the confidence of investors, facilitating access to both domestic and foreign capital. Companies adhering to sound governance practices tend to exhibit superior financial performance and a greater capacity to attract foreign investment, elements that are crucial for the diversification of the Cape Verdean economy, fostering sectors such as technology and innovation. Moreover, corporate governance promotes responsible and efficient management practices, which are essential for sustainable development. Transparency and accountability, the cornerstones of corporate governance, are vital for the integrity of business operations, mitigating the risks of corruption and mismanagement, and bolstering the confidence of investors and the broader business environment within Cape Verde.

As can be readily observed, the significance of corporate governance transcends mere statutory compliance, functioning as a strategic resource for the sustainable development of both Cape Verde and its constituent companies. The integration of Environmental, Social, and Governance (ESG) factors into corporate governance structures constitutes a strategic imperative for ensuring long-term sustainability and competitiveness within the global marketplace. Companies in Cape Verde are increasingly acknowledging that the transition towards an economic development model predicated on sustainability engenders inevitable shifts in the manner in which company value will be assessed. Furthermore, the adoption of commendable corporate governance practices has demonstrably served as a catalyst for investor confidence, improved access to capital, and enhanced operational efficiency, thereby contributing to sustainable development and the strengthening of the nation's capital market.

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The Duty of Loyalty of Administrators in the CSCV: Ethical, Legal, and Fiduciary Dimensions

The duty of loyalty stands as one of the fundamental pillars of corporate governance, mandating that administrators act in good faith and in the best interests of the company at all times. Article 79 of the CSCV explicitly stipulates that the members of the administrative organs must conduct themselves *“with the diligence of a prudent and orderly manager and with loyalty, in the interest of the company”*. This duty imposes a mode of conduct oriented towards the corporate interest, rendering inadmissible the personal exploitation of business opportunities or the advocacy of interests that are antagonistic to those of the company. The interpretation and application of this duty within Cape Verde are informed by prevailing international best practices. Any conduct deviating from this standard may even provide grounds for a civil liability action.

In its ethical dimension, the duty of loyalty necessitates that administrators act with probity and good faith, prioritising the interests of the company above their own personal interests. From a legal standpoint, this duty entails the obligation to safeguard the company’s assets and to promote its commercial objectives. From a fiduciary perspective, the duty of loyalty reflects the trust reposed in the administrators by the company and its diverse array of stakeholders. The pertinence of the duty of loyalty extends to the protection of the interests not solely of the shareholders but also of other entities crucial to the company’s sustainability, such as employees, clients, and creditors. A transparent, efficient, and responsible administration, firmly anchored in the duty of loyalty, is indispensable for fostering confidence within the markets, among investors, and among the shareholders themselves.

The Regime of Conflicts of Interest in the Cape Verde Commercial Companies Code

The CSCV dedicates particular attention to the subject of conflicts of interest, establishing a comprehensive legal regime that is aligned with international principles of corporate governance. Article 79, in addition to establishing the duty of loyalty, imposes upon administrators the obligation to communicate to the company any situations that may potentially constitute a conflict of interest. Moreover, the CSCV outlines several specific prohibitions and restrictions designed to forestall the occurrence of conflict situations. For instance, the granting of loans or any form of credit to administrators, as well as the provision of guarantees for their obligations or the provision of salary advances exceeding one month’s remuneration, is expressly prohibited.

Conversely, Article 80 declares null and void any clause that purports to exclude or limit the liability of administrators for breaches of their duties, as well as any clause that makes the initiation of a liability action contingent upon prior authorisation. This provision underscores the significance of holding administrators accountable and prevents them from shielding themselves against legal proceedings arising from the non-fulfilment of their responsibilities. It is also pertinent to note that Article 83 recognises the legitimacy of shareholders holding at least 5% of the share capital to initiate a social liability action, even in instances where the company itself has not pursued such action. This mechanism is intended to counteract situations of institutional inertia or the capture of supervisory bodies, thereby ensuring the protection of the interests of minority shareholders.

While the CSCV does not furnish an exhaustive enumeration of situations that may give rise to conflicts of interest, certain common examples

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warrant highlighting. These include the execution of contracts between the company and its administrators (self-dealing), instances of dual representation wherein an administrator represents two contracting companies, and participation in deliberations that involve the direct economic interests of the administrators or individuals related to them. In all such cases, the administrator is obligated to abstain from participating in the deliberation, failing which they may incur civil liability. By way of illustration, the utilisation of company resources for personal enrichment, engagement in business activities that compete with the company, and the making of decisions that favour related parties to the detriment of the company's interests constitute typical scenarios of conflict of interest.

The ramifications of conflicts of interest that are not adequately managed can be considerable for companies, encompassing the erosion of investor confidence, damage to reputation, regulatory scrutiny, and potential legal penalties. The proactive identification and management of conflicts of interest, through the implementation of clear policies, disclosure requirements, and recusal procedures, are indispensable for mitigating these risks and ensuring ethical and transparent governance.

In this context, the CSCV assigns a significant role to the supervisory body (Fiscal Council) in the prevention and repression of conflicts of interest. Its actions are expected to be proactive, and it is even empowered to judicially seek the annulment of flawed corporate resolutions. The Fiscal Council bears the responsibility of overseeing the administration of the company, ensuring compliance with the law and the articles of association, and verifying the accuracy of the financial statements. The existence of an independent Fiscal Council, comprising mem-

bers with elevated standards of professional diligence and loyalty, serves as an important safeguard of transparency and accountability.

The success of the legal regime governing conflicts of interest hinges, to a considerable extent, on the presence of an organisational culture that places a premium on ethics, integrity, and accountability. The CSCV establishes the necessary normative framework, but it falls to the companies themselves to implement compliance policies, codes of conduct, whistleblowing channels, and training programs for their administrators and employees. In essence, the Cape Verdean legislator has explicitly linked the existence of a robust conflict of interest regime to enhanced investor confidence within the local market.

Furthermore, it is essential that the administrative bodies are adequately equipped to identify reputational risks, prevent instances of misconduct, and foster an internal culture of transparency and responsibility. The encouragement of the establishment of ethics committees and the periodic conduct of internal audits can further reinforce this institutional commitment.

The analysis of the treatment of conflicts of interest and the duty of loyalty within the CSCV reveals a congruity with numerous best practices and international recommendations pertaining to corporate governance. The OECD Principles of Corporate Governance, for example, underscore the importance of disclosure, restrictions on certain transactions, and the role of supervisory bodies in the management of conflicts of interest. Cape Verde's approach, as reflected in the CSCV, aligns with many of these principles, particularly in its emphasis on disclosure, restrictions on specific transactions, and the function of the supervisory body.

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The adoption and effectiveness of these norms have a direct impact on the confidence of both domestic and foreign investors. When investors see that companies are subject to clear regulations that prevent managers from pursuing personal gain to the detriment of the company, the sense of legal security and integrity is enhanced. With well-defined duties of loyalty in place, the risk of administrators entering into transactions that would be detrimental to the company (for example, contracting with themselves or related entities on unfavourable terms) is reduced. The legal requirement for the approval and disclosure of related-party transactions inhibits the practices of self-dealing and other forms of abuse. The obligation to disclose conflicts and the prohibition against voting on matters in one's own interest lend transparency to the management of the company. This transparency is highly valued by investors, as it allows them to assess whether the management is acting in an ethical manner.

Investors – particularly foreign investors, who are often less familiar with the local business environment – seek out markets where legal security prevails. The knowledge that the legislation imposes clear fiduciary duties on administrators and provides mechanisms for accountability in cases of infringement allows for predictability. Foreign investors feel more assured that they will receive fair treatment, and that any potential disputes can be resolved based on objective

rules (for example, if a director breaches their duty of loyalty, causing harm, the company or shareholders can seek redress). This confidence reduces perceived country risk and can translate into a greater propensity for investment. Concurrently, domestic investors also gain the confidence to allocate their resources to local public limited companies, being aware that the rights of all shareholders will be safeguarded by the legal framework.

The adoption of legal standards that are aligned with international norms (such as those promulgated by the OECD and the World Bank) serves as a positive signal. It indicates that the country takes the protection of investors and the integrity of the business environment seriously. This renders the market more appealing.

Drawing inspiration from international models, such as the OECD Principles of Corporate Governance and the European Union directives on corporate governance, Cape Verde has the potential to forge its own path towards the affirmation of sound practices, tailored to its specific dimensions and economic context. This adaptation, however, necessitates not merely the transposition of legal norms but also the creation of enabling conditions for their realisation, through investments in training, technical capacity building, the modernisation of information systems, and the enhancement of internal control bodies.

CANADA

Law and Practice

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Fasken is an internationally recognised law firm with over 950 lawyers and ten offices across three continents. The firm is trusted by clients to provide practical and innovative legal services, solving complex business and litigation challenges while prioritising client needs. Fasken's team is vigilant in monitoring the global regulatory landscape and advising clients on relevant changes that may impact policy development and business practices. With offices in London, Johannesburg and across Canada, as well as alliances with firms worldwide, boards, committees and executives often seek Fasken's advice on various matters, including proposed trans-

actions, post-merger leadership, crisis management, internal investigations, disclosure, proxies, stakeholder relations and engagement, whistle-blowing, board recruitment, and the development of governance policies and practices. The firm's practice areas cover a wide range of legal specialties including M&A and capital markets, competition and antitrust, ESG, government relations, insolvency and restructuring, intellectual property, international trade, labour, employment and human rights, litigation and dispute resolution, privacy and cybersecurity, procurement, and tax.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The principal form of business organisation in Canada is the business corporation which affords shareholders limited liability protection, and Canada has 14 different business corporations statutes under which these can be incorporated. The Canada Business Corporations Act (CBCA) is Canada's federal business corporations statute. Each of Canada's 13 provinces and three territories also has its own business corporations statute. However, these are generally modelled on the CBCA such that, in most cases and subject to limited exceptions (such as director residency requirements), there is generally little substantive difference among them practically speaking. Several provincial business corporations statutes in Canada provide for unlimited liability corporations, which may be advantageous as part of cross-border tax planning (but which do not necessarily provide shareholders the same extent of limited liability protections that business corporations do).

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance requirements in Canada are the business corporations statute under which the company is incorporated and, if the company is publicly listed in Canada, Canadian securities laws. Also, while not technically binding or obligatory, corporate governance practices in Canada can be significantly impacted by various non-legal sources such as proxy advisory firm recommendations and contemporary industry best practices.

A particularly notable non-legal source of corporate governance practice in Canada is the

potential influence of Canadian institutional investors such as pension funds. Many of these investors have distinct expectations regarding various corporate governance matters, including as relates to such issues as diversity, equity and inclusion (DEI) and sustainability, and they can proactively exert pressure on their portfolio companies towards these ends. This pressure can sometimes be significant, including where institutional investors together hold a sizeable shareholding and because many Canadian public companies are not as widely-held as more often occurs in certain other jurisdictions.

Overall, corporate governance in Canada continues to evolve and is an area of acute interest among companies, investors, regulators and other market participants.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Publicly traded companies in Canada are subject to various corporate governance rules and guidelines of both mandatory and voluntary application. Mandatory requirements are imposed principally by the company's governing corporate statute (see **1.1 Forms of Corporate/Business Organisations**) or by applicable securities laws. Voluntary requirements result principally from non-legal sources such as the expectations of institutional investors (eg, pension funds; see **1.2 Sources of Corporate Governance Requirements**), proxy advisory firm recommendations, and contemporary industry best practices.

Notwithstanding the 14 different corporations statutes (federal, provincial and territorial; see **1.1 Forms of Corporate/Business Organisations**) available in Canada, the majority of Canadian public companies are incorporated

under the CBCA. This makes the CBCA the most relevant Canadian corporations statute when discussing the corporate governance of Canadian public companies. Regarding securities laws, Canada does not have a national securities regulator similar to the Securities and Exchange Commission (SEC) in the United States. Instead, each province and territory generally has its own securities statutes and securities regulators. That said, there is significant harmonisation among these various securities laws, including further to the work of the Canadian Securities Administrators (CSA), which is an umbrella organisation of Canada's provincial and territorial securities regulators whose mandate is to improve, co-ordinate and synchronise the regulation of Canadian capital markets.

The two principal Canadian stock exchanges are the Toronto Stock Exchange (TSX) and the TSX Venture Exchange (TSXV) and each of these have listing rules. However, these rules do not factor prominently as relates to corporate governance matters, which are generally left to Canadian corporate law and securities law.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

There are several current “*hot topics*” in corporate governance in Canada. These include (i) economic uncertainty posed by trade and tariff policies, (ii) diversity, equity and inclusion (DEI) matters, (iii) relatively new legislation addressing forced labour and child labour in supply chains, and (iv) relatively new legislation imposing corporate transparency and disclosure obligations. For discussion of “*hot topics*” involving ESG considerations, including regarding climate change disclosure, see **2.2 ESG Considerations**.

Economic uncertainty posed by the evolving trade and tariff policies of the new US administration is creating risks of varying degrees for different Canadian companies. The challenge for Canadian boards is to respond appropriately as warranted by the company's particular exposure and risk profile, including, for example, more regular meetings with management to discuss response strategies.

DEI is another area of recent focus for the CSA (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**). In early 2023, it published for comment a proposed rule that would require enhanced disclosure from non-venture issuers regarding how the issuers identify and evaluate new candidates for nomination to a company's board and how diversity is incorporated into those considerations. In particular, the CSA sought input on (i) whether the enhanced regime should require specific disclosure with respect to Indigenous peoples, LGBTQ2SI+ persons, racialised persons, persons with disabilities, or women, or (ii) whether the specific disclosure should be limited to women on a company's board and allow for voluntary disclosure with respect to other under-represented groups. In April 2025, the CSA announced it was pausing this matter to (i) support Canadian markets and issuers as they adapt to recent developments in the global and geopolitical landscape (ie, trade and tariff uncertainty), and (ii) focus on initiatives to make Canadian capital markets more competitive, efficient and resilient. However, the CSA also stated it expects to revisit the matter in the future. See also **6.2 Disclosure of Corporate Governance Arrangements**.

Regarding forced or child labour in supply chains, Canada's Fighting Against Forced Labour and Child Labour in Supply Chains Act

(FCLA) entered force in January 2024. The FCLA requires covered entities to file annual reports addressing the risk of forced or child labour in their supply chains, both in Canada and internationally. The reports must also address the company's related due diligence processes and employee training, if any. Covered entities include companies listed on a Canadian stock exchange or doing business in Canada that meet at least two of the following three thresholds for at least one of the last two financial years: at least (i) CAD20 million in assets, (ii) CAD40 million in revenue, and/or (iii) 250 employees.

Regarding corporate transparency, several Canadian corporate statutes (see **1.1 Forms of Corporate/Business Organisations**) now require the disclosure of information regarding individuals with significant control over privately owned companies. For example, the CBCA requires the identification of any person owning or controlling 25% or more of the company's shares, whether individually or together with related persons. This has been the case since 2019. However, in 2024 the CBCA was amended to add a federal register of individuals with such significant control, parts of which register are publicly available. The aim of the disclosure is to assist authorities in fighting money laundering, tax evasion and similar illegal activities, and the legislation includes whistle-blower protections. Penalties for non-compliance include a maximum fine of CAD1 million.

For further discussion, including recent developments in ESG or sustainability reporting, see **2.2 ESG Considerations**.

2.2 ESG Considerations

ESG reporting in Canada remains fluid as public companies continue to consider how best to approach ESG disclosure and build reliable

internal systems to address evolving stakeholders' demands.

Key issues in ESG reporting in Canada have recently included:

- board oversight, where boards are taking a more active role in ESG oversight, with increasing involvement from audit committees;
- executive compensation, where some companies are incorporating ESG metrics into their short-term executive compensation decisions;
- reporting frameworks, where sustainability reports are becoming a key tool for ESG disclosure and with companies referencing one or more frameworks in their reporting;
- assurance, where companies are increasingly obtaining third-party assurance (typically limited assurance) for specific ESG disclosures;
- greenhouse gas (GHG) reporting, where some companies are addressing GHG emissions reduction targets;
- indigenous engagement, where some Canadian public companies are disclosing policies focused on engagement and reconciliation, particularly companies in Canada's resources and finance sectors (see also **2.1 Hot Topics in Corporate Governance**);
- forced labour and child labour, where Canada's Fighting Against Forced Labour and Child Labour in Supply Chains Act has recently entered force; and
- shareholder proposals, where Canada's financial services industry receives the most ESG-related shareholder proposals.

Relatedly, the authors have begun witnessing the ESG disclosure of Canadian public companies shift from employing "ESG" terminology to broader "sustainability" terminology.

It remains unclear whether Canadian securities regulators will impose mandatory climate-related disclosure. Such requirements had been under development and were expected to be released toward the end of 2025. However, in April 2025 the CSA announced it was pausing this matter to (i) support Canadian markets and issuers as they adapt to recent developments in the global and geopolitical landscape (ie, trade and tariff uncertainty), and (ii) focus on initiatives to make Canadian capital markets more competitive, efficient and resilient. However, the CSA also stated it expects to revisit the matter in the future. The CSA also reminded reporting issuers that climate-related risks are *“mainstream business issue and securities legislation already requires issuers to disclose material climate-related risks affecting their business in the same way that issuers are required to disclose other types of material information”*.

A related notable development is the passage of significant changes to Canada’s Competition Act requiring companies to substantiate representations regarding the environmental or climate benefits of their products, services or business activities. This includes the introduction (beginning in June 2025) of a private right of action regarding greenwashing claims. Since the passage of the legislation, some Canadian companies have responded by reducing or withdrawing related voluntary ESG disclosure.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The management of Canadian companies is principally conducted by the CEO, CFO and the other members of the executive management team. The authority of management is as del-

egated to management by the board of directors. Best practice in Canada is for the board to devise a formal mandate for itself together with an associated delegation of authority to management.

3.2 Decisions Made by Particular Bodies

Best practice in Canadian corporate governance is for shorter term and general operational decision-making to be delegated by the board to management and for the board to retain authority over longer term and *“bigger picture”* issues. Matters over which the board retains authority are often allocated to board committees.

Audit committees are required at Canadian public companies. The committee must be composed of a minimum of three members and, subject to limited exceptions, each member must be independent.

Other common committees include a compensation committee, a corporate governance committee, an environmental or ESG committee, a nominating committee, a disclosure committee, a pension committee, a risk committee, a safety committee and/or a finance committee. The number and nature of committees formed by the board is generally a function of the size of the company and the nature of its business. Best practice is for a committee to be comprised of board members who have expertise in the particular area of the committee’s mandate.

Special board committees are typically formed in certain circumstances, such as in connection with a possible change of control transaction (eg, an unsolicited takeover bid), in relation to an internal investigation (eg, regulatory non-compliance), or in response to an emergency or crisis situation (eg, a data breach).

3.3 Decision-Making Processes

Canadian corporate law limits the board's ability to delegate its authority in that certain decisions are within the sole authority of the directors. For example, under the CBCA, only the board may (i) submit to shareholders matters requiring their approval, (ii) declare dividends, (iii) approve financial statements for distribution to shareholders, (iv) approve a management proxy circular, takeover bid circular or other circular, or (v) amend or repeal the company's by-laws. However, committees can (and often do) advise on these matters before the full board makes a final decision.

Even where it is legally permissible to delegate decision-making to a board committee or management, best practice in Canada is for the board to carefully consider whether to do so. Typically, matters of strategic importance or material policy, while sometimes at first instance the responsibility of a committee, are reserved for final determination by the board (eg, after the committee has made its recommendations). For example, while risk committees have become common at large Canadian public companies, ultimate authority over the "risk-reward" balance to be assumed at the enterprise level is often reserved for the full board.

4. Directors and Officers

4.1 Board Structure

Canada's business corporations statutes prescribe basic requirements regarding board structure. Private companies are generally required to only have a single director. Public companies are generally required to have a minimum of three directors, at least two of which are not officers or employees of the company or its affiliates. Typically, a public company's articles will allow

for a range in the number of directors so that the board can be expanded or reduced as circumstances warrant and without having to amend the company's articles. In order to fulfil its duties, a board should have sufficient directors for its own direct needs and to serve on the board's committees.

4.2 Roles of Board Members

The allocation of roles and responsibilities among board members is generally approached on a case-by-case (ie, company-specific) basis in Canada. Best practice is to develop and implement a formal mandate for the board, which includes a considered delegation of authority to management. Best practice in Canada is also for the board to continually evaluate which specific skill sets are most relevant to its needs and which of those might be absent and thus should be added.

4.3 Board Composition Requirements/Recommendations

Several of Canada's business corporations statutes impose residency requirements. For example, under the CBCA, a minimum of 25% of the company's directors must be resident Canadians. For requirements relating to board size, see **4.1 Board Structure**. For requirements relating to director independence, see **4.5 Rules/Requirements Concerning Independence of Directors**. In addition, public companies are required to have audit committees composed of directors that are independent directors (see **4.5 Rules/Requirements Concerning Independence of Directors**) and that are financially literate.

4.4 Appointment and Removal of Directors/Officers

In Canada, shareholders elect the company's directors at the company's AGM or at a special meeting called, in whole or in part, for the

election of directors. Directors are generally removed either by being replaced at a subsequent AGM or by resolution at a special meeting held between AGMs. Majority voting applies to uncontested elections at companies governed by the CBCA or listed on the TSX or other non-venture exchanges. The board appoints the company's officers and these officers serve at the pleasure of the board.

4.5 Rules/Requirements Concerning Independence of Directors

There are different definitions of “*independence*” as it relates to corporate governance in Canada. The CBCA provides that a director is independent if they are not employed by the company or any of its affiliates. Canadian securities laws define independence as the lack of “*material relationship*” with the company.

A material relationship is defined as one which could be reasonably expected to interfere with the exercise of independent judgement. Certain relationships are automatically deemed to be material, including being a current or recent executive officer (or other employee) of the company or being a current or recent partner (or employee) of the company's auditor.

Canadian securities laws also require that public companies disclose which directors are independent and which are not. Where a majority of the board does not qualify as independent, the company must disclose what the board does to ensure the independent exercise of judgement in fulfilling its duties. Canadian securities laws also require that all members of an audit committee are independent and provide guidance (which is adhered to by almost all public companies) that all members of a compensation committee should be independent.

Directors must disclose the nature and extent of any conflict of interest they have in a material contract or material transaction, whether made or proposed, with the company where the director (i) is a party to the contract or transaction, (ii) is a director of a party to the contract or transaction, or (iii) has a material interest in a party to the contract or transaction. Subject to limited exceptions (see **4.10 Approvals and Restrictions Concerning Payments to Directors/Officers**), the director cannot vote on any board resolution relating to the contract or transaction.

For a discussion of key legal issues related to nominee directors, see **5.1 Relationship Between Companies and Shareholders**.

4.6 Legal Duties of Directors/Officers

The principal legal duties of officers and directors under Canadian corporate law are twofold: the duty of care and the duty of loyalty.

Satisfying their duty of care in managing the company requires that officers and directors exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. This includes the officers and directors sufficiently informing themselves and considering all related material information before taking action.

Satisfying their duty of loyalty in managing the company requires that officers and directors act honestly and in good faith with a view to the corporation's best interests. They must act impartially and free of self-interest or self-dealing and always put the company's best interests first, regardless of any competing or conflicting interests, including their own or of any of the company's shareholders.

Importantly, and unlike in certain other jurisdictions, neither the duty of care nor the duty of loyalty can be waived, whether in the company's articles, by contract or otherwise. That said, as further discussed at **5.1 Relationship Between Companies and Shareholders**, such duties can be partially or wholly transferred from the officers and directors to the company's shareholders by the functioning or express terms of a unanimous shareholders' agreement governing the company.

4.7 Responsibility/Accountability of Directors

Canadian law is clear that directors owe their duties to the company and not to any of its stakeholders, including shareholders. However, the CBCA and a substantively similar ruling by the Supreme Court of Canada (Canada's highest court) provide that, in pursuing the company's best interests, directors may take into account, without limitation, (i) the interests of shareholders, employees, retirees and pensioners, creditors, consumers and governments, (ii) the environment, and (iii) the corporation's long-term interests.

Directors and officers in Canada also benefit from the "*business judgement rule*." This provides that, so long as the company's directors and officers act honestly, in good faith, and with a reasonable degree of care and diligence, Canadian courts will not second-guess their business decisions, even where those decisions ultimately result in negative consequences for the company. Stated differently, the business judgement rule recognises that directors and officers often face complex and uncertain business situations, and thus should be afforded a degree of discretion in making decisions without fear of personal liability, provided they act in pursuit of the cor-

poration's best interests and within the scope of their authority.

4.8 Consequences and Enforcement of Breach of Directors' Duties

As the duties of care and loyalty are owed by directors and officers to the company, a claim for breach of these duties lies with the company. However, and as further discussed at **5.4 Shareholder Claims**, Canadian corporate law allows for derivative actions whereby a shareholder can pursue a claim against the directors or officers on behalf of the company for a breach of duty owed by them to the company.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

As further discussed at **5.4 Shareholder Claims**, the actions of directors and officers may give rise to an oppression claim under Canadian corporate law, which is a broad and potentially powerful statutory remedy. That said, Canadian courts have held the fundamental purpose of the oppression remedy is to provide recourse regarding actions taken by the company. As such, the actions of the directors or officers will generally only be oppressive when they are acting in their capacity as directors and officers, and the claim is against the company as opposed to the directors.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The CBCA expressly permits directors to vote on their own remuneration as directors, notwithstanding the conflict of interest. That said, management typically provides significant input into the compensation process, including by considering recent "*comparables*" and/or by engaging compensation advisers. Canadian securities guidelines recommend that the company's com-

pensation committee is ultimately responsible for making recommendations on director compensation, and this best practice is generally followed. “Say-on-pay” shareholder proposals have been common for Canadian public companies for several years. “Say-on-pay” votes by shareholders (ie, non-binding advisory votes) are not yet mandated by securities law or the CBCA but have been voluntarily adopted by many large public Canadian companies.

4.11 Disclosure of Payments to Directors/Officers

Canadian securities law requires the disclosure of the process followed in deciding director and officer remuneration. This should include explanation of the board’s process, the rationale for the board’s decision, and why the remuneration is otherwise appropriate or justified. Best practice includes also disclosing the frequency and form of compensation. This disclosure of officer remuneration is required to be included in the Compensation Discussion and Analysis portion of a public company’s proxy circular.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The relationship between a Canadian company and its shareholders is governed primarily by the company’s business corporations statute (federal, provincial or territorial; see **1.1 Forms of Corporate/Business Organisations**).

Generally speaking, shareholders in a Canadian company do not owe any fiduciary duties or other duties to the company. Nor do shareholders in Canadian companies owe any fiduciary duties or other duties to other shareholders of the company. A possible exception is where the

company’s shareholders have entered a unanimous shareholders’ agreement (USA) in which case, to the extent the USA limits or otherwise restricts the authority of the directors to manage the company, the related duties and liabilities of the directors will be transferred from the directors to the shareholders. Caution should also be exercised where a shareholder nominates a director to the company’s board, as the nominee director will owe duties to the company without regard to any duties they may owe to the nominating shareholder in any other capacity.

Canadian corporations statutes generally provide that shareholders who dissent regarding shareholder votes on specified fundamental matters can compel the company to acquire their shares at fair value, a process referred to as “*dissent and appraisal rights*”. A prominent example is where the shareholder dissents in relation to a squeeze-out transaction. It is also typical for shareholders to be granted dissent and appraisal rights in connection with a proposed plan of arrangement effecting any negotiated (ie, “*friendly*”) acquisition of the company.

Lastly, the principle of separate corporate personality is a fundamental rule of Canadian law. As such, a shareholder will only be liable for the company’s actions should a court rule it appropriate to “*pierce the corporate veil*”. Due to the very high standard generally imposed in such claims – eg, where the company is used to perpetrate a fraud, this occurs relatively infrequently in Canada.

5.2 Role of Shareholders in Company Management

The principal role of shareholders in the management of the company is their right to elect the company’s directors (see **4.4 Appointment and Removal of Directors/Officers**). The approval of

shareholders is also required to effect various fundamental changes. These generally include (i) amendments to the company's articles or by-laws, (ii) transactions involving substantially all of the company's assets or property, (iii) a merger (referred to as an "*amalgamation*" in Canada) of the company with another company, (iv) a migration or "*continuation*" of the company under another governing corporations statute, and (v) dissolution of the company.

Beyond the foregoing, shareholders of Canadian companies may also be entitled to (i) make a shareholder proposal, and (ii) requisition a shareholder meeting.

Regarding shareholder proposals, these can generally be made by a shareholder owning a minimum 1% interest and require that the company include the proposal in a management proxy circular being distributed by the company. The proposal and its supporting statement cannot exceed 500 words. Shareholder proposals in Canada are typically made in connection with a company's AGM. Note, however, that where the shareholder proposal relates to the election of one or more directors, a minimum 5% interest is generally needed.

Regarding requisitioning a shareholder meeting, this can be done by one or more shareholders owning a minimum 5% interest. This is most commonly done by shareholder activists as part of a proxy campaign to elect a dissident slate of directors. Requisitioning a shareholder meeting requires strategic planning and careful compliance with various technical requirements. Also, even where a shareholder meeting has been requisitioned, it is not uncommon for Canadian courts to allow the subject matter of the requisitioned meeting to be deferred to

the next scheduled shareholder meeting (ie, the company's AGM).

While shareholders in Canadian companies do not benefit from approval rights regarding the vast majority of the company's business decisions, practically speaking a dialogue often occurs between public companies and their largest investors. In Canada, this is particularly so regarding public companies and their institutional shareholders (eg, pension funds). This reflects the fact that Canadian institutional investors often own (either individually or in groups) large blocks of shares in Canadian public companies. This can give the institutional investor(s) outsized influence on the company compared to other jurisdictions where public companies may be more widely held than many public companies in Canada. See also **1.2 Sources of Corporate Governance Requirements**.

5.3 Shareholder Meetings

Canadian companies are required to hold an AGM. This must occur not later than 15 months following the last AGM or six months following the company's most recent financial year. AGMs and other shareholder meetings are conducted in accordance with the company's by-laws.

The principal business conducted at AGMs in Canada is (i) the election of the company's board of directors, (ii) presentation of the company's financial statements and the report of the company's auditors on the financial statements, and (iii) the appointment of the company auditor. "*special meeting*" is a meeting called for the purpose of conducting business other than the foregoing – eg, a meeting requisitioned by an activist shareholder.

Although shareholders of Canadian public companies are entitled to attend AGMs in person,

they more commonly vote by proxy. Since the COVID-19 pandemic, it has become increasingly common for shareholder meetings in Canada to be held virtually. As such, several Canadian corporations' statutes have been amended to expressly address virtual meetings as well as to impose rules companies must satisfy in conducting such meetings. Guidance has also been issued by Canadian securities regulators regarding their expectations for virtual meetings held by Canadian public companies. Most recently, several shareholder proposals have related to returning to in-person annual shareholder meetings, with an option to attend virtually, and have received majority support.

Where a matter to be addressed at a shareholders' meeting is subject to a shareholder vote, the matter must be comprehensively described in a management information circular made available to shareholders in advance of the meeting. This circular must include, among other things, the recommendation of the company's board regarding the matter. For example, where a Canadian public company has negotiated a change of control transaction whereby it is to be acquired, the company will send to shareholders proxy materials and a meeting circular containing the board's recommendation in advance of a meeting called for shareholders to vote on the transaction.

5.4 Shareholder Claims

Canadian corporate law provides for three main varieties of shareholder claims. These are (i) a personal action, (ii) a derivative action, and (iii) an oppression claim.

A personal action seeks to enforce rights personal to the shareholder. One instance in which personal actions are more common is in the context of a shareholder activist campaign. For

example, the activist may seek a court order compelling the requisitioning of a shareholder meeting where the company has refused to act. Similarly, an activist can resort to court action to challenge the company's invocation of its advance notice by-laws amid a proxy contest and the activist's attempted nomination of a dissident slate of directors. Other examples of rights personal to a shareholder include the right to vote, the right to timely and informative notice of meetings, and the right to inspect the company's books and records.

A derivative action is where the shareholder seeks to pursue a claim not in its own name but on behalf of the company. The classic example of a derivative action is a claim against the company's directors for breach of their fiduciary duties. To bring a derivative action, the shareholder must first obtain the court's approval. This generally requires satisfying three conditions. First, that the shareholder must have given at least 14 days' notice to the company of its intent to bring the derivative action if the company does not bring the applicable claim itself. Second, the shareholder must convince the court that it is acting in good faith in bringing the claim. Third, the shareholder must convince the court that its proposed claim is in the company's best interests.

An oppression claim is unique to Canadian corporate law and is a broad and potentially powerful statutory remedy, including as it grants the court wide discretion in devising any resulting relief. In brief, an oppression claim enables shareholders – as well as other security holders, creditors, directors or officers – to seek judicial intervention where they believe the company (or its directors or officers) have acted in a manner that is oppressive or unfairly prejudicial or that unfairly disregards the claimant's interests. Con-

duct that can give rise to oppression includes actions contrary to the company's governing documents, actions contrary to the directors' fiduciary duties, and/or actions that disregard or undermine the claimant's legal rights or interests. Unlike a derivative action, a shareholder need not first seek court approval to bring an oppression claim with the result that an oppression claim (or the threat of an oppression claim) is often the first recourse of a disaffected shareholder in Canada.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Disclosure obligations can arise for shareholders in Canadian public companies in several different circumstances.

Canadian securities laws generally require that "insiders" of Canadian public companies file reports disclosing information regarding transactions involving the company's securities. The term "insider" is broadly defined and includes persons who have significant influence over the company and/or routine access to material undisclosed company information. This also includes the company's officers and directors (as well as those of the company's subsidiaries) and the company itself where it has purchased, redeemed or otherwise acquired some of its own securities and significant shareholders (ie, 10% shareholders). Insider reports must disclose, among other things, (i) the insider's direct or indirect beneficial ownership of, or control or direction over, company securities, and (ii) any change to the foregoing. Separate and supplementary insider reporting requirements exist for derivatives. Various exemptions from Canadian insider reporting requirements are available depending on the circumstances.

Should a shareholder acquire a 10% or more interest in a Canadian public company, the early warning reporting (EWR) system under Canadian securities laws is triggered. This requires that the shareholder (i) issue a news release before the opening of trading on the next business day, (ii) file an early warning report within two days of the 10% threshold being crossed, and (iii) not acquire additional shares from the time the reporting requirement is triggered until at least one business day after the early warning report is filed. Prescribed information for disclosure includes the amount of the shareholding and the shareholder's investment intent. Additional news releases and early warning reports are required thereafter (i) each time the shareholder increases or decreases its shareholding by 2% or more, (ii) for every change in material information contained in a previously filed report, and (iii) should the shareholder's ownership percentage fall below the 10% threshold. The reporting threshold under the EWR system drops from 10% to 5% if the public company becomes the target of a takeover bid.

The Investment Canada Act (Canada) and Competition Act (Canada) have thresholds for the acquisition of shares (33.33% and 20% respectively) of a Canadian public company that could trigger considerations under these statutes. Finally, any acquisition of shares in a Canadian public company by a shareholder that, together with the shareholder's current interest (if any), would bring the shareholder's interest to 20% or more must comply with Canada's takeover bid regime.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Canadian public companies are required to file several annual financial reports. These include the following.

- Annual and Quarterly Financial Statements including the company's income statement, balance sheet, statement of changes in equity and cash flow statement.
- Annual and Quarterly Management's Discussion and Analysis (MD&A) which provides management's analysis of the company's financial condition, results of operations and future prospects.
- An Annual Information Form (AIF) that details the company's operations, management, governance structure and risk factors.
- A Proxy Circular distributed in advance of the company's AGM that provides information to shareholders regarding matters subject to a shareholder vote – eg, the election of directors and auditor appointment.
- Annual and Quarterly CEO/CFO certifications of the accuracy and completeness of the company's financial statements and disclosures.

6.2 Disclosure of Corporate Governance Arrangements

Canadian securities laws have, since 2005, required the disclosure of certain public company corporate governance practices, including as relates to (i) board composition and independence, (ii) the board's mandate, (iii) ethical business conduct and codes, (iv) the continuing education of directors, (v) the nomination process for directors, (vi) the compensation process for directors, and (vii) standing board committees. Canadian securities regulators have also issued

related guidelines for corporate governance disclosure best practices.

In 2014, most Canadian jurisdictions (ie, provinces and territories; see **1.2 Sources of Corporate Governance Requirements**) adopted requirements that non-venture Canadian public companies disclose their policies and targets for female representation on their boards and in executive officer positions, as well as the number and proportion of women in those roles. In 2021, Canadian public companies governed by the CBCA became required to disclose prescribed information regarding "*designated groups*", being women, Aboriginal people, members of visible minorities and persons with disabilities. In 2023, the CSA published alternative amendments for public comment that could impose additional corporate governance disclosure requirements regarding persons from specifically identified groups. Overall, corporate governance disclosure requirements and best practices in Canada continue to evolve.

6.3 Companies Registry Filings

The registry filings required by a Canadian company are as prescribed by the company's governing corporate statute. For example, under the CBCA these include (i) an Annual Return detailing the company's registered office address, directors, and officers, and (ii) prompt filing of any changes to information included in an Annual Return. Failure to comply with these filing requirements can result in penalties, administrative dissolution or other adverse consequences. As discussed at **2.1 Hot Topics in Corporate Governance**, as of 2024, CBCA companies must file information regarding individuals with significant control over the company, some of which information will be publicly available.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Canadian private companies generally have the option regarding whether or not to appoint an external auditor, and often waive this requirement. Public companies in Canada must appoint an external auditor and the auditor must meet independence requirements. It is not uncommon for large Canadian public companies to have an auditor independence policy which, among other things, establishes a process for determining whether the audit and other services provided by the external auditor to the company affect its independence vis-à-vis the company.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Unlike Delaware corporate law, Canadian corporate law does not expressly provide for “*Caremark*” claim – ie, where a plaintiff can file suit where a company’s board either failed to properly implement an internal system of reporting and controls for key risks facing the company or, having established such an internal system, failed to properly monitor it. Nonetheless, instituting an effective enterprise risk management system is best practice in Canada, as a failure to do so could potentially give rise to a breach of duty of care claim against the company’s directors (see 4.6 Legal Duties of Directors/Officers). It is therefore common for large Canadian public companies to have one of their committees address enterprise risk considerations and regularly report to the full board.

Trends and Developments

Contributed by:

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Introduction

Corporate governance in Canada continues to evolve. Diversity continues to be a focus of regulatory and proxy advisory policy change, and for boards, is a key component of ESG concerns. The adoption of majority voting in the Canada Business Corporations Act (CBCA) strengthens shareholders' hands at shareholder meetings. The introduction of legislation governing disclosure of beneficial ownership of company shares, as well as certain other matters not previously subject to mandatory disclosure, are showing a trend towards increased transparency. Climate change is another core aspect of ESG concerns at the board level. Proposed climate-related disclosure rules will entail very significant changes to corporate governance that will require boards of directors to undertake a comprehensive review of the corporation's governance structures and practices. Changes continue to be made to corporate statutes to remove perceived technical burdens. Stakeholders will look for more oversight from the board as adoption of generative artificial intelligence (AI) continues to grow exponentially.

Diversity – Boards and Senior Management

Diversity on boards and in senior management is being reviewed by corporate regulators and stakeholders, and the legal and “soft law” requirements have and are continuing to evolve. Since 2014, Toronto Stock Exchange (TSX)-listed corporations have been required to make diversity-related disclosure in their annual disclosure documents on “*comply or explain*” basis, including:

- on their policies and targets regarding the representation of women on the board of directors and in executive positions;

- how the representation of women is considered in selecting board and executive officer candidates;
- gender representation on the board and in executive officer positions; and
- term limits.

See National Instrument 58-101 of the Canadian Securities Administrators (CSA) Disclosure of Corporate Governance Practices (NI 58-101).

Public corporations existing under the CBCA have been required to make diversity-related disclosure regarding women, indigenous peoples, persons with disabilities and members of visible minorities (designated groups) since 2020 on “*comply or explain*” basis. These requirements include:

- disclosure of term limits or other board renewal mechanisms, a description of written diversity policies for the selection of individuals from designated groups as board nominees and a description of progress made in achieving the policy objectives;
- whether the level of representation of designated groups on the board or in senior management is considered in appointing new candidates;
- whether targets have been established for representation of designated groups on the board and in senior management, as well as progress towards those targets; and
- the number of members of each of the designated groups on the board and in senior management.

Enhanced guidelines for making this disclosure were published by Corporations Canada in February 2022.

Increasingly, governance ratings organisations and industry groups developing “*best practices*” are focusing on gender and other diversity measures as critical elements of measuring/rating corporate governance. See, for example, the Canadian Coalition for Good Governance (CCGG) and The Globe and Mail Board Games.

Proxy advisory firms are following suit, with both Glass, Lewis & Co (Glass Lewis) and Institutional Shareholder Services (ISS) adopting gender diversity policies in respect of Canadian public corporations (regardless of jurisdiction of incorporation).

Glass Lewis has updated its voting policies with respect to board gender diversity effective for shareholder meetings on or after 1 January 2025, as set out below.

- Glass Lewis maintains a percentage-based approach to board gender diversity and will generally recommend voting against the nominating committee chair of any TSX-listed company board that is not at least 30% gender diverse, as well as all members of the nominating committee of a board with no gender diverse directors. Glass Lewis defines “*gender diverse directors*” as women and directors that identify with a gender other than male or female.
- For companies listed on junior exchanges, Glass Lewis’ minimum threshold remains at one gender diverse director.
- Glass Lewis may refrain from recommending that shareholders vote against the election of directors of companies when boards have provided a sufficient rationale or plan to address the lack of diversity on the board.

Beginning with shareholder meetings held after 1 February 2025, the ISS voting guidelines have changed as follows.

- ISS will recommend against the election of the chair of the nominating committee, or its equivalent, of a company listed on the S&P/TSX Composite Index with less than 30% representation of women on its board of directors.
- ISS has amended one of the exceptions to the requirement that boards of S&P/TSX Composite Index issuers be comprised of at least 30% women. Assuming there is a publicly disclosed written commitment to achieve 30% representation of women on the board at or before the subsequent annual general meeting (AGM), an exception will be made for companies that have fallen below the 30% threshold after achieving such level at the preceding AGM.
- Previously, companies could only take advantage of this exemption if they fell below the 30% threshold due to an extraordinary circumstance. ISS has now removed the reference to “*extraordinary circumstances*”.
- For TSX-listed companies which are not also included in the S&P/TSX Composite Index, ISS will generally vote against the election of the chair of the nominating committee, or its equivalent, if there are zero women on the board of directors.

In 2024, ISS broadened its policy on diversity beyond gender to include requirements for racially and/or ethnically diverse board members (defined as Aboriginal peoples, meaning persons who are indigenous, Inuit or Métis, and members of visible minorities, meaning persons other than Aboriginal peoples, who are non-Caucasian in race or non-white in colour).

For meetings on or after 1 February 2025, for companies in the S&P/TSX Composite Index, ISS continues to recommend to vote against or withhold from the Chair of the Nominating Committee or Chair of the committee designated with the responsibility of a nominating committee, or the Chair of the board of directors if no nominating committee has been identified or no chair of such committee has been identified, where the board has no apparent racially or ethnically diverse members. If the board has provided a formal, publicly disclosed written commitment to add at least one racially or ethnically diverse director at or prior to the next annual meeting, an exemption will be made for companies that have:

- joined the S&P/TSX Composite Index and were not previously subject to the racial/ethnic board requirement at the previous AGM; or
- fallen below the minimum racial or ethnic representation on the board after achieving such level of representation at the previous AGM.

Federally-incorporated issuers are required to report on diversity among the “*members of senior management*” (as defined in the regulations). The CBCA requires CBCA-incorporated issuers to provide certain “*prescribed information*”, which includes, but is not limited to, reporting on whether the board of directors or its nominating committee have considered the level of representation in management roles of “*designated groups*”. The designated groups are defined as: women, indigenous peoples (First Nations, Inuit and Métis), persons with disabilities and members of visible minorities.

The Employment Equity Act Review Task Force has recommended updates to modernise the Employment Equity Act (Canada) (EEA) with

respect to diversity reporting. Key changes include:

- replacing the term “*designated groups*” with “*employment equity groups*”;
- introducing terms like “*racialized workers*” and “*Indigenous peoples*”; and
- creating new designated categories for Black workers and 2SLGBTQI+ workers.

While no legislative changes have been proposed for the CBCA, the Canadian government has expressed support for these recommendations and has planned consultations to modernise the EEA. Any amendments to the EEA could influence future CBCA diversity reporting. The consultation period regarding the recommendations closed on 30 August 2024.

Securities regulators in Canada continue to focus on diversity disclosure requirements. In January 2021, the Capital Markets Modernization Taskforce, established by the Ontario government, issued its final report suggesting, among other things, that:

- Ontario securities legislation be amended to require that Canadian public companies set goals and implement timelines for diversity amongst directors and executive management, and report annually on the levels of representation at the board and executive management of those identifying as women, BIPOC, a person with a disability or LGBTQ+; and
- appropriate target levels for representation be at 50% for women and 30% for BIPOC, persons with disabilities and LGBTQ+.

Additionally, on 30 October 2024, staff of the CSA published Multilateral Staff Notice 58-317 – Review of Disclosure Regarding Women on

Boards and in Executive Officer Positions, the tenth annual review by the CSA on disclosure regarding women on corporate boards and in executive officer positions. The CSA reported a small increase, as compared to its prior year's report, in the overall percentage of women on boards and in executive officer positions.

On 13 April 2023, the CSA proposed amendments to Form 58-101F1 – Corporate Governance Disclosure and National Policy 58-201 – Corporate Governance Guidelines pertaining to diversity, board renewal and board nominations. The CSA proposed two versions of Form 58-101F1 for comment, “Form A” and “Form B”, which are applicable to non-venture issuers.

Form A

Form A requires disclosure on an issuer's approach to diversity in respect of the board and executive officers but would not mandate disclosure in respect of any specific groups, other than women.

For example, an issuer would disclose its chosen diversity objectives, how progress is measured, and the mechanisms in place to achieve these objectives.

This can be achieved by collecting data with respect to specific groups the issuer identifies as being relevant for its approach to diversity and for comparative purposes.

There is no required format on how to present this information; the approach taken in this form is intended to provide each issuer with flexibility to design practices and policies respecting how it will address diversity in its specific circumstances, and not requiring it to report data on any specific group.

Form B

Form B requires disclosure on the representation of five designated groups, being:

- women;
- indigenous peoples;
- racialised persons;
- persons with disabilities;
- LGBTQ2SI+ persons; and
- persons on boards and in executive officer positions.

An issuer may also choose to voluntarily provide disclosure in respect of other groups beyond the foregoing designated groups.

All such data would be reported in a standardised tabular format to promote consistent and comparable disclosure. This information would be based on voluntary self-disclosure by directors and executive officers.

In addition, this form would require disclosure regarding any written strategy, written policies and measurable objectives relating to diversity on an issuer's board of directors.

The key difference between the two forms is that Form B mandates disclosure on historically underrepresented groups, which is a similar approach to the board diversity disclosure requirements under the CBCA. In contrast, Form A mandates disclosure only on women's representation and is based on a view that securities regulators should not select categories of diversity. Form A defers to an issuer to determine what additional categories or aspects of diversity they wish to implement based on the company's business and strategy. Under the same notice, the CSA has also proposed enhanced guidelines for issuers relating to board nominations and renewals. In April 2025, the CSA announced

that it was pausing its review of stakeholders' comments from the consultation period on its new approaches towards diversity disclosure. No timeline has been provided for any restart of this initiative.

On 15 February 2025, the Department of Finance proposed rules for distributing federally regulated financial institutions (FRFIs) under the Bank Act, Trust and Loan Companies Act, and Insurance Companies Act. These proposed regulations will mandate federally regulated financial institutions, including banks, to disclose the diversity composition of their boards and senior management. The consultation period for the Diversity Information Disclosure Regulations ended on 17 March 2025. It remains to be determined when the new regulations will come into force.

Transparency – Beneficial Ownership

Recent beneficial ownership disclosure requirements are showing a trend towards increased transparency, with the goal of assisting law enforcement agencies in targeting potential money laundering and tax evasion.

Effective 1 January 2023, the Business Corporations Act (Ontario) (OBCA) was amended to require certain private corporations existing under the OBCA to prepare and maintain a register of individuals with “*significant control*” over the corporation. Under the OBCA, an individual with significant control is someone who:

- is the registered or beneficial owner of, or has direct or indirect control or direction over, any number of shares that carry 25% or more of the voting rights attached to all of the corporation's outstanding voting shares;
- is the registered or beneficial owner of, or has direct or indirect control or direction over, any number of shares that is equal to 25% or

more of all of the corporation's outstanding shares measured by fair market value;

- has any direct or indirect influence that, if exercised, would result in control in fact of the corporation; or
- is an individual to whom circumstances prescribed by regulation apply.

Certain groups, such as individuals with jointly held rights or interests in shares, who are parties to a voting or similar arrangement, and/or having certain familial relationships, are considered on a collective basis towards meeting the threshold test for significant control; where a group has met the test, all members are required to be disclosed.

For each individual with significant control, the register must include the following information per the OBCA:

- name, date of birth and last known address;
- jurisdiction of residence for tax purposes;
- the date on which the individual became (or ceased to be) an individual with significant control;
- description of how the individual meets the definition of significant control;
- any other information that may be provided for in regulations enacted in the future; and
- a description of the steps taken to identify all individuals with significant control and to ensure that the information in the register is accurate, complete and up to date.

The amendments to the OBCA are similar to other corporate transparency initiatives introduced by the CBCA and in the provinces of British Columbia, Saskatchewan, Manitoba, Nova Scotia, PEI, Newfoundland and Labrador and, most recently, Quebec. Effective 31 March 2023, the Act respecting the legal publicity of

enterprises (LPE) requires certain companies to submit information about their “*beneficial owners*” to the *Registraire des entreprises du Québec* (REQ). The amended LPE requires the disclosure of “*ultimate beneficiaries*”, which is generally defined as a natural person who holds a right that allows them to benefit from a portion of the income or assets of an enterprise, or a right that allows them to direct or influence the activities of the enterprise. Registrants must provide the REQ with the following information on the ultimate beneficiaries:

- first and last name (or name if the ultimate beneficiary is a legal person) and other names used in Quebec;
- date of birth;
- residential address;
- the type of control exercised, including the holding percentage where applicable; and
- the date on which the person became an ultimate beneficiary and, if applicable, the date on which the person ceased to be one.

As of 22 January 2024, the CBCA was amended with respect to disclosure of beneficial ownership to, among other things:

- require the director (as defined under the CBCA) to make available to the public certain information on individuals with significant control over a corporation;
- protect the information and identity of certain individuals;
- add, or broaden the application of, offences and provide the director with additional enforcement and compliance powers; and
- add regulatory authority to prescribe further requirements in certain provisions. It also makes consequential and related amendments to other Acts.

Transparency – Say-on-Pay Vote

Upcoming amendments to the CBCA would require the directors of prescribed corporations to annually disclose their approach to remuneration and to provide shareholders with a non-binding “*say-on-pay*” vote. The CBCA amendments (under proposed Section 172.4) are passed, but not yet in force. The Ontario Capital Markets Modernization Taskforce has also suggested a number of changes including mandating an annual advisory “*say-on-pay*” similar to the CBCA requirements. Many public companies already voluntarily provide their shareholders with “*say-on-pay*” vote.

Glass Lewis maintains its voting policies with respect to shareholder opposition to “*say-on-pay*” proposals and a board’s level of engagement and responsiveness to shareholder concerns.

Where Glass Lewis finds that a company’s compensation policies and practices serve to reasonably align compensation with performance, and such practices are adequately disclosed, Glass Lewis will recommend supporting the company’s approach. If, however, those specific policies and practices fail to demonstrably link compensation with performance, Glass Lewis will generally recommend voting against the say-on-pay proposal.

Glass Lewis generally expects a board’s minimum appropriate level of responsiveness to correspond to the level of shareholder opposition (in a single year and over time) and may recommend holding compensation committee members accountable for failing to adequately respond to shareholder opposition, having regard for the level of opposition and history of the company’s compensation practices.

Furthermore, Glass Lewis will take a holistic approach when analysing executive compensation programmes and not use a pre-determined scorecard approach when considering individual features. Glass Lewis reviews unfavourable factors in a pay programme in the context of rationale, overall structure, overall disclosure quality, the programme's ability to align pay with performance, and the trajectory of the programme as a result of changes introduced by the compensation committee.

Transparency – Incentive Awards and Clawback Policies

A clawback policy allows an employer to reclaim compensation previously paid to employees. Clawback policies typically relate to compensation paid under incentive-based plans to certain executives and are typically administered by a company's compensation committee or board of directors for the purpose of responding to changing financial metrics. Clawback policies may also extend to incentive-based compensation based on non-financial results of the company (ie, safety, retention and production). Many public companies have already established clawback policies.

Effective 2 October 2023, the United States Securities and Exchange Commission has adopted new amendments and rules governing clawback policies, establishing standards that needed to be adapted by companies listed on the New York Stock Exchange and Nasdaq by 1 December 2023. The CBCA, under proposed Section 172.3, could also require a company to disclose prescribed information about the recovery of incentive benefits paid to directors and employees who are members of senior management.

Innovation, Science and Economic Development Canada (ISED) provided further guidance on the prescribed information outlined in the proposed CBCA amendments. ISED explains that the prescribed information should follow “*disclose or explain*” regime where companies indicate whether they have a clawback policy, and if not, the reasons why they have not adopted one. If the company does have a policy, it will be required to disclose the policy's objectives and key provisions.

Starting from 2023, Glass Lewis has raised concerns about executive pay programmes where less than half of an executive's long-term incentive awards are subject to performance-based vesting conditions. As with the past years, Glass Lewis may refrain from a negative recommendation in the absence of other significant issues with the programme's design or operation, but performance-based awards that are significantly rolled back or eliminated from a company's long-term incentive plan may be viewed negatively.

Glass Lewis continues to support clawback or “*malus*” provisions in 2025 to safeguard against unwarranted short-term and long-term incentive awards.

In situations where a company determines not to follow through with financial recovery from an executive officer, Glass Lewis will assess the appropriateness of such determination for each case. A thorough, detailed discussion of the company's decision to not pursue recoupment and, if applicable, how the company has otherwise rectified the disconnect between executive pay outcomes and the shareholder experience will be considered. The absence of such enhanced disclosure may impact Glass Lewis' assessment of the quality of disclosure and, in turn, may play a role in Glass Lewis' overall rec-

ommendation for the advisory vote on executive compensation. The clawback provision should provide recoupment authority regardless of whether the employment of the executive officer was terminated with or without cause.

The CCGG also encourages the use of clawback policies to monitor performance-based compensation.

Transparency – Board Matters

Glass Lewis has noted the importance of companies providing substantive disclosure about the experience and expertise of board nominees. Where the disclosure of an issuer in the S&P/TSX 60 Index is not sufficient to allow for a meaningful assessment of the key skills and experience of incumbent directors and board nominees, Glass Lewis may recommend voting against the chair of the nominating committee, or its equivalent.

Glass Lewis may now issue a negative voting recommendation in respect of the chair of the governance committee of a TSX-listed issuer, or the most senior member of the committee in the absence of a chair, if the governance committee did not meet at least once during the year in review.

ISS has clarified that former CEOs of a TSX-listed issuer will be deemed non-independent unless there are exceptional circumstances to reassess this classification after a minimum cooling-off period of five years. ISS will continue to recommend against any director who has served as a former CEO and is a member of the audit or compensation committee unless ISS classifies such director as independent following the cooling-off period. This recommendation also applies to a director who has served as a CFO within the past three years.

Transparency – Voting “For” or “Against” Directors of Public Corporations

Canadian corporate statutes have historically required that shareholders either vote for or withhold their vote on the election of directors at annual meetings. This has meant that if a director receives just one vote for their election at an uncontested shareholder meeting, then that director will be elected, even if a vast majority of shares are withheld from voting for that director.

Starting in 2014, all corporations listed on the TSX were required to adopt a majority voting policy pursuant to which each director must be elected by a majority of votes cast with respect to their election, except at a contested meeting. Majority voting policies must also require:

- a director to immediately tender their resignation if they are not elected by at least a majority (50% +1 vote) of the votes cast with respect to their election;
- the board to determine whether to accept the resignation within 90 days of the shareholder meeting, and the resignation should be accepted in the absence of exceptional circumstances;
- the resignation to become effective when accepted by the board;
- a director who tenders a resignation not to participate in board or committee meetings at which the resignation is considered; and
- the issuer to promptly issue a news release with the board’s decision including, in the case of a board not accepting the resignation, the reasoning behind such a decision.

On 31 August, 2022, amendments to the CBCA came into force that changed the majority voting requirements for board nominees, as set out below.

- CBCA-incorporated public corporations must allow shareholders to vote “for” or “against” individual director nominees in an uncontested election, rather than “for” or “withhold”.
- Where only one nominee is up for election for each board seat and less than 50% of the votes cast by shareholders are “for” particular director nominee, such a nominee will not be elected as a director (subject to provisions in the issuer’s articles). However, if an incumbent director is not elected by a majority of “for” votes at the meeting, they will still be permitted to remain as a director until the earlier of: (i) the 90th day after the day of the election; or (ii) the day on which their successor is appointed or elected.
- The elected directors may reappoint the incumbent director even if they do not receive majority support in the most recent election in certain limited circumstances:
 - (a) where it is required to satisfy the CBCA’s Canadian residency requirement; or
 - (b) where it is required to satisfy the CBCA’s requirement that at least two directors of a distributing corporation are not also officers or employees of the corporation or its affiliates.

Preparing for Mandatory Climate-Related Disclosure – Governance Changes for Public Corporations

On 18 October 2021, the CSA published a proposed National Instrument 51-107 – Disclosure of Climate-related Matters and its proposed Companion Policy 51-107CP (together, the Climate Disclosure Proposals) for comment.

The Climate Disclosure Proposals would require disclosure based on recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD). The Climate Disclosure Proposals

would require issuers to make disclosure in the following areas.

- Governance – describing the board’s oversight of climate-related risks and opportunities, and management’s role in assessing and managing climate-related risks and opportunities.
- Strategy – describing any climate-related risks and opportunities identified over the short, medium and long term and describing the impact of these risks and opportunities on its business, strategy and financial planning.
- Risk management – describing its processes for identifying, assessing and managing climate-related risks and how these processes are integrated into overall risk management.
- Metrics and targets – describing its metrics used to assess climate-related risks and opportunities and targets used to manage these risks and opportunities.

The TCFD contemplates that issuers should disclose greenhouse gas emissions (Scope 1, 2 and 3). The Climate Disclosure Proposals would require issuers to make this disclosure or explain why they do not. The Climate Disclosure Proposals would not require issuers to disclose the resilience of their strategy with reference to various climate scenarios, a key element of the TCFD recommendations.

In preparing to comply with the new requirements, corporations and boards should be taking the following steps.

- Boards of directors should expressly establish oversight of climate-related risks and opportunities of the issuer. This will require reviewing, and where necessary amending, board charters and mandates and board skills and competencies matrices, and then review-

ing whether any changes need to be made in board composition to ensure the board has the necessary climate competencies to effectively provide this oversight.

- Boards of directors should expressly task management with responsibility for assessing and managing climate-related risks and opportunities. This will involve the review and revision of role descriptions and mandates. As climate-related disclosure is added to an issuer's management information circular, annual information form (AIF) or management's discussion and analysis (MD&A), the annual and interim CEO/CFO certifications (National Instrument 52-109 Certification of Disclosure in an Issuer's Annual and Interim Filings) will apply to that climate-related disclosure. Management will need to have designed disclosure controls and procedures to provide reasonable assurance that climate-related material information will be made known to the CEO and CFO, and that required disclosure on climate-related matters is made. Boards of directors will need to be comfortable that these controls and procedures are in place and have oversight over their effectiveness.
- Boards of directors should consider board committee roles in the review and assessment of climate-related risks. Boards of directors should consider the mandates of any board committees that have delegated responsibilities around risk review and assessments, and carefully consider where the assessment of climate risks should fit within those board committees, if at all.
- Boards of directors should specifically consider the role of the audit committee in the review and assessment of climate-related risks and opportunities. The assessment of climate-related risks and opportunities is likely to be done within existing enterprise risk management systems, often overseen by the audit committee. At a minimum, the audit committee will need to ensure that once climate-related risks and opportunities are assessed, their implications are properly reflected in the issuer's financial reporting including in assumptions, uncertainties and estimates made in the preparation of financial statements.
- Boards of directors should be aware that the Climate Disclosure Proposals require climate-related disclosure to be contained in documents that by law must specifically be reviewed and approved by the board (namely, the corporation's AIF, management proxy circular and, in some cases, the MD&A). Climate-related disclosure is often made in standalone sustainability or other reports.
- Boards of directors will need to assess the materiality of climate-related risks and opportunities. The Climate Disclosure Proposals require an issuer to disclose:
 - (a) climate-related risks and opportunities (short, medium and long-term) and their impact on the issuer's businesses, strategy and financial planning (Strategy);
 - (b) the issuer's processes for identifying, assessing and managing climate-related risks (Risk Management); and
 - (c) metrics and targets used by an issuer to assess and manage climate-related risks and opportunities (Metrics and Targets) only where the information is "material" ie, where a reasonable investor's decision to buy, sell or hold securities is likely to be influenced if the information is omitted or misstated.
- Boards of directors should consider the need for scenario analysis as contemplated within the TCFD recommendations. They should consider whether in order to properly identify climate-related risks and opportunities, and

their impact on an issuer's business, management needs to undertake some scenario analysis as contemplated within the TCFD recommendations notwithstanding that the Climate Disclosure Proposals do not require disclosure in respect of those scenarios. In turn, boards would need to review that analysis. The use of scenario analysis as a tool to assess risks and opportunities is generally understood to offer benefits in situations where the precise timing and magnitude of risks are uncertain, the analysis needs to be forward-looking, and risks (and opportunities) can be high impact where historical experience is not necessarily a guide to the likelihood of their future occurrence.

- Boards of directors will need to consider the annual timing of preparation of an issuer's climate-related disclosure. Currently, many issuers are reporting this type of information in standalone sustainability reports and/or other documents released throughout the year on different schedules from the typical annual disclosure cycle.
- Boards of directors should consider any de facto requirement to disclose GHG emissions. They should consider whether there will develop (or maybe already has developed in some cases) a de facto requirement to disclose GHG emissions in their disclosure documents, notwithstanding that the Climate Disclosure Proposals adopt "*comply or explain*" model allowing issuers to omit that disclosure if they explain why. Access to the various sustainable finance tools or funding from some institutional investors may already require that an issuer discloses its GHG emissions. If issuers enter into sustainability-linked financings based on GHG emissions, they will be reporting their GHG emissions to banks and bond holders. Canada's largest banks (and other Canadian and international finan-

cial institutions) have established net zero emissions targets. To satisfy these requirements, it seems likely issuers will face more general requirements to provide this GHG emissions disclosure to their banks. Many issuers are already providing GHG emissions information in investor presentations or in separate sustainability reports. Where investors and other stakeholders are asking for this data, it becomes harder to argue the information is not "*material*".

- Boards of directors should consider whether the issuer should start early in addressing the disclosure contemplated by the Climate Disclosure Proposals.
- Boards of directors will need to monitor the development of climate disclosure ratings and rankings established by third parties. As has occurred in respect of general governance disclosure (see, for example, the CCGG and The Globe and Mail Board Games), benchmarking of issuers' climate-related disclosure has started. See, for example, the Climate Action 100+ corporate benchmarking which looks at corporate disclosures around climate-related governance, reduction of GHG emissions and public disclosure following the TCFD recommendation. These rankings (and their score cards) are likely to become a consideration in the preparation of issuers' public disclosure documents.

Since the CSA's Proposed Climate Disclosure Proposals, the International Sustainability Standards Board (ISSB) has issued a climate-related disclosure standard as well as a general standard for sustainability-related financial information (ISSB Standards). The Canadian Sustainability Standards Board (CSSB) has also issued its climate-related disclosure standard and general sustainability standard (CSSB Standards), which are substantively the same as

the ISSB Standards except for few transitional matters relating to Scope 3 emissions, quantitative scenario analysis and the general timing of disclosure. The ISSB Standards and the CSSB Standards are voluntary standards.

Following the release of the CSSB Standards, the CSA announced that it would continue to work toward a revised climate-related disclosure rule and would consider the CSSB Standards with modifications appropriate for the Canadian capital markets. In April 2025, the CSA announced it was pausing its work toward a revised climate-related disclosure rule, but encouraged companies to use the CSSB Standards if they were making voluntary sustainability disclosure. No timeline has been provided to restart this work.

ISS and Glass Lewis have climate accountability voting policies that address climate-related disclosure and board oversight of climate-related issues. Effective for shareholder meetings held after 1 February 2025, and under its *“Climate Accountability Policy”*, the ISS will generally vote against or withhold from the incumbent chair of the appropriate committee (or other directors) of companies that are significant GHG emitters (ie, companies identified by the Climate Action 100+) and do not: (i) make adequate climate-related risks disclosure in line with the four-pillar framework established by the TCFD; or (ii) adopt appropriate GHG emissions targets.

Glass Lewis will assess whether climate-related disclosures are aligned with the recommendations of the TCFD at TSX 60 companies with material exposure to climate risk. It will also assess whether these companies have disclosed explicit and clearly defined board-level oversight responsibilities for climate-related issues. If these are absent or significantly lacking, Glass Lewis may recommend voting against

the chair of the committee (or board) charged with oversight of climate-related issues, or if no committee has been charged with such oversight, the chair of the governance committee.

Similar to ISS, and effective for shareholder meetings held after 1 January 2023, Glass Lewis has adopted *“Board Accountability for Climate-related Issues”* policy under which it will make negative voting recommendations for the chair of the relevant committee (or board) of high-emitting companies (ie, whose GHG emissions represent a financially material risk, including companies identified by the Climate Action 100+) that do not: (i) provide thorough TCFD-aligned disclosure; or (ii) clearly define board oversight responsibilities for climate-related issues. The Glass Lewis policy may be extended to the chair of the governance committee where no committee (or board) has been assigned oversight of climate-related issues and could also apply to other directors. The group of companies to which the Glass Lewis policy applies appears to be broader than for the ISS policy. Glass Lewis believes that boards of high-emitting companies should have explicit and clearly defined oversight responsibilities for climate-related issues, which builds on broader Glass Lewis and ISS policies requiring board-level oversight of environmental issues and disclosure of such oversight.

The Ontario Teachers’ Pension Plan, one of Canada’s largest investors, continues to advocate for strong climate oversight in its 2025 Proxy Voting Guidelines. The 2025 Guidelines maintain heightened expectations of Audit Committees, including climate literacy as a core competency for its members. Climate-related impacts must be evaluated when reviewing budgets, performance and M&A activity. Additionally, the Audit Committee should understand environmental

and related reporting requirements for companies.

In May 2024, Senator Julie, Miville-Dechéne introduced the 21st Century Business Act (Bill S-285). Bill S-285 is a Senate public bill that proposed to amend the CBCA to incorporate social and environmental obligations into corporate duties and decision-making. In particular, Bill S-285 sought to:

- mandate directors and officers of CBCA companies to consider prescribed stakeholder constituencies, including the environment, when determining the best interests of the corporation; and
- require annual reporting of a corporation's social and environmental impact.

On 6 January 2025, Bill S-285 was terminated due to the prorogation of the Parliament of Canada. It remains to be determined whether the public bill will be re-introduced in the new session.

Shareholder Meetings and Materials

The debate concerning the format of shareholder meetings continues. Past legislative amendments have introduced flexibility for companies with respect to shareholder meetings, such as the following.

On 31 May 2022, amendments to the Business Corporations Act (Alberta) (ABCA) came into force adjusting the notice period of shareholder meetings for Alberta private corporations to a minimum of seven days and a maximum of 60 days (formerly, minimum of 21 days and maximum of 50 days). The amendments under the ABCA also permit corporations to send documents required to be sent to directors and shareholders by electronic means.

On 1 October 2023, changes to the OBCA relating to shareholder meetings came into force. These changes expressly allow virtual shareholder meetings (under Section 94 (2)) and also allow companies to determine the manner by which shareholder meetings are held (under Section 94 (3)(a)).

On 22 February 2024, the CSA provided updated guidance on virtual shareholder meetings after providing initial guidance in February 2022. The guidance focuses on disclosure concerning shareholder access and participation at virtual meetings, and shareholder participation at virtual meetings.

In terms of disclosure, the CSA suggests that reporting issuers provide:

- clear and comprehensive disclosure in management information circulars and associated proxy-related materials concerning the logistics for accessing, participating and voting at a virtual shareholder meeting;
- full explanations of the registration, authentication and voting process for shareholders;
- shareholders with information concerning the procedures for how shareholder questions will be received and addressed, and how shareholder participation will otherwise be accommodated and managed at the meeting; and
- contact information where shareholders can obtain assistance in the event of difficulties during the registration process or while accessing and attending the meeting.

In terms of shareholder participation, the CSA suggests reporting issuers to provide for a level of shareholder participation at a virtual meeting that is comparable to that which a shareholder could reasonably expect if they were attending an in-person meeting. This would include oppor-

tunities to make motions or raise points of order, and the ability to raise questions and provide direct feedback to management in any question and answer segment of the meeting. Proponents of shareholder proposals accepted to be voted on at the meeting should typically also be given the opportunity to speak to the proposal.

Glass Lewis has clarified its expectations that companies should engage with their shareholders when determining the format for their annual shareholder meetings. When in-person attendance is not permitted, companies must provide a rationale for this choice. While Glass Lewis does not have a policy based solely on shareholder meeting format, it may recommend voting against the chair of the governance committee, or another relevant director, where the board has failed to sufficiently respond to legitimate shareholder concerns regarding the meeting format.

Similar to Glass Lewis, ISS raises concerns about virtual-only shareholder meetings. ISS recommends voting against proposals to amend or adopt the company's articles or by-laws to include a provision that gives the directors discretion to hold virtual-only shareholder meetings without compelling rationale.

The CCGG has also expressed concerns about virtual-only shareholder meetings and advocates for hybrid or in-person meetings.

Written Resolutions of Shareholders

Corporate statutes in Canada have long contemplated that shareholders can sign written resolutions in lieu of holding a shareholder meeting. Typically, these resolutions need to be signed by all shareholders to be valid, and so have been a helpful tool for closely held corporations. On 28 March 2023, amendments to the ABCA came into force allowing for written resolutions signed

by holders of at least two thirds of the shares entitled to vote at the shareholder meeting to be valid as if passed at a meeting. The reduced threshold is eligible only for private Alberta Corporations, and brings the ABCA into alignment with other corporate statutes in Canada (such as in Ontario and British Columbia) that permit non-unanimous written resolutions.

Canadian Director Residency Requirements

Canadian corporate statutes have required that a certain percentage (typically 25%) of the directors of a corporation be Canadian residents. "*Canadian resident*" has been defined to include Canadian citizens and permanent residents, in each case, who are ordinarily resident in Canada.

In March 2023, the Business Corporations Act, 2021 (Saskatchewan) was amended to remove the Canadian resident director requirement. In its place, corporations without a director or officer who is a Saskatchewan resident must designate an attorney in Saskatchewan. The Saskatchewan amendment is in line with the majority of Canadian provinces and territories including British Columbia, Alberta, Ontario, Quebec, Nova Scotia and New Brunswick.

Interlocking Directorships

Glass Lewis believes that a board should be wholly free of people having identifiable conflicts of interest. It generally recommends that shareholders withhold votes from affiliated or inside directors where the director has an interlocking relationship with one of the company's executives. Top executives serving on each other's boards creates an interlock that poses conflicts that should be avoided to ensure the promotion of shareholder interests above all else.

Glass Lewis also considers interlocking relationships with close family members of executives

or within group companies, and may also determine that conflicts of interest exist. Further, it also reviews multiple board interlocks among non-insiders (ie, multiple directors serving on the same boards at other companies) for evidence of a pattern of poor oversight.

Glass Lewis has expanded its policy on interlocking directorships to consider both public and private companies.

Board Oversight of AI

As generative AI continues to grow with an unprecedented speed of adoption, it is accompanied with demand from stakeholders for board oversight and guardrails. Regulators across the globe are exploring legislation that would curtail the use of certain types of AI. In 2023 in the US, for the first time there were shareholder proposals calling for disclosure on the board's oversight of AI and ethical guidelines on the use of AI.

Davies Governance Insights 2024 suggests that boards and management can take a number of actions to address such concerns, including: (i) understanding the use cases of current AI technology for the business; (ii) understanding the risks inherent in the use of AI technology; and (iii) developing an AI governance policy to help address current risks and to provide a framework to address what is yet to come.

On 5 December 2024, the CSA published "*Staff Notice and Consultation 11-348 – Applicability of Canadian Securities Laws and the Use of*

Artificial Intelligence Systems in Capital Markets" to clarify how existing securities laws apply to the use of AI systems by participants in capital markets. The CSA identified "*AI washing*" as a disclosure deficiency and a form of overly promotional disclosure which can be misleading to the public or constitute a misrepresentation.

Effective for shareholder meetings held after 1 January 2025, Glass Lewis has established a new policy addressing board oversight of AI. Glass Lewis believes issuers that use or develop AI technologies should adopt strong internal frameworks that include ethical considerations, ensure effective oversight of AI, and expect clear disclosure on how boards are overseeing AI. To ensure effective oversight, Glass Lewis recommends that boards engage in continued board education to expand their collective expertise and understanding in this area and/or appoint directors with AI expertise.

Glass Lewis believes that clear disclosure on how boards are overseeing AI and expanding their expertise is likely to be of value to shareholders. While Glass Lewis will not make voting recommendations solely based on a company's AI oversight practices and disclosure, it may recommend against the re-election of accountable directors if there is evidence that insufficient management of AI technology has resulted in "*material harm*" to shareholders.

CHILE



Law and Practice

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Clyde & Co Chile is the Santiago office of Clyde & Co, a dynamic international law firm with over 2,400 lawyers and 3,200 legal professionals operating from over 60 offices and associated offices in six continents. It focuses on providing a complete legal service to businesses and governments around the world in its core sectors of insurance, construction, transport, energy, infrastructure and trade and commodities. Its globally integrated teams provide a com-

prehensive range of legal services and advice to businesses operating at the heart of global trade and commerce. The multidisciplinary team brings together a dedicated group of experienced professionals, with expertise across diverse practice areas, and has a robust understanding of the regulatory and policy drivers of the market, and extensive experience through a wide range of sectors, contexts, in solving problems and providing practical solutions.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Under Chilean law, business entities fall broadly into two categories: capital companies and partnerships. Partnerships have minimal regulatory requirements, which is why this overview focuses on capital companies - such as Corporations (*Sociedades Anónimas* or S.A.s) and By-Stock Companies (*Sociedades por Acciones* or SpAs) - which are subject to more extensive legal and compliance obligations. Where relevant, partnerships, including Limited Liability Companies (Ltdas), which remain in use despite their more rigid structure, will also be addressed.

Capital Companies

In capital companies, the central element is the capital contribution of the shareholders. These entities are formed primarily to pool resources, rather than based on the identity of their members. Shareholders are interchangeable and their liability is limited to the capital they contribute. The main types of capital companies include the following.

Corporation (*Sociedad Anónima*, or S.A.)

Corporations are the most regulated form of legal entity in Chile. Their key features include:

- a strict governance structure, often requiring a board of directors;
- mandatory annual shareholder meetings and minimum dividend distributions; and
- detailed reporting and operational obligations, especially for those under regulatory oversight.

There are three types of corporations:

- Listed corporations: these must register their shares with the Financial Market Commission (*Comisión para el Mercado Financiero*, or CMF) either by legal mandate or because they meet specific criteria (eg, a large number of shareholders). They are publicly traded and subject to intense regulatory scrutiny.
- Closed corporations: these are privately held, with simpler rules for share transfer and lower reporting burdens. They must convert into listed corporations if they meet legal thresholds for public offering.
- Special corporations: certain industries - such as banking, insurance, and pensions - require specific corporate forms. These entities are subject to sector-specific regulation and CMF oversight.

By-stock companies (*sociedad por acciones* or SpA)

SpAs are a flexible, modern vehicle for business incorporation in Chile. They combine limited liability with simplified corporate governance and are often chosen for their adaptability. Key features include:

- capital divided into shares;
- freedom to define governance structures in the by-laws, including whether to appoint a board or another managing body;
- simplified procedures for issuing new shares or bringing in new investors; and
- those incorporated by a single shareholder, unlike corporations (S.A.) and limited liability companies (Ltdas), which require at least two founding members.

Law No. 18,046 on Corporations applies on a supplementary basis to SpAs in areas not expressly governed by their by-laws and the Code of Commerce, particularly regarding direc-

tors' duties, shareholder rights, and governance standards.

SpAs have largely replaced limited liability companies for new businesses, due to their flexibility and investor-friendly design.

Partnerships

In partnerships, the emphasis is on personal identity and trust among partners (the *affectio societatis*). Capital contributions matter less than the personal bond between partners. These entities typically involve limited transferability of interest, meaning new partners can only be admitted with unanimous consent, and liability is often limited to capital contributions, although rules can vary. Additionally, they exhibit a strong dependence on the ongoing participation of the founding partners.

The most common form is the Limited Liability Company. Traditionally favoured before the rise of SpAs, Ltdas require unanimous partner consent for changes and may dissolve upon a partner's exit, unless otherwise agreed in the by-laws.

1.2 Sources of Corporate Governance Requirements

Corporate governance in Chile is structured by a mix of statutory laws, administrative regulations, and voluntary frameworks. The main sources of legal requirements for capital companies include:

- Law No. 18,046 (Corporations Law or LSA), which regulates the structure, management, and shareholders' rights in corporations.
- Law No. 18,045 (Securities Market Law or LMV), which sets standards for listed companies and securities markets, including disclosure and transparency obligations.

- Decree Law No. 211 of 1973 (Free Competition Law or LPLC), overseen by the National Economic Prosecutor's Office (FNE): this law promotes market transparency and prevents anti-competitive conduct.
- Law No. 19,913, which establishes the Financial Analysis Unit (*Unidad de Análisis Financiero*, or UAF) and introduces anti-money laundering and counter-terrorism financing controls.
- Law No. 21,000, which creates the Financial Market Commission (*Comisión para el Mercado Financiero*, or CMF), supervising market conduct and compliance.
- Administrative regulations issued by the CMF and UAF, which include detailed rules on corporate governance, reporting, and compliance systems.

Sector-specific regulations apply to industries such as banking, insurance and pensions, which must meet heightened corporate governance standards under their own legal regimes.

Additionally, Law No. 20,393 introduces corporate criminal liability and mandates companies to adopt compliance programs, including crime prevention models and environmental risk controls.

Beyond statutory requirements, companies may adopt non-governmental standards, such as ESG guidelines, stock exchange listing rules, or self-regulatory codes. These frameworks aim to enhance transparency, ethical conduct and sustainability in corporate governance.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Listed companies with publicly traded shares are subject to heightened regulatory standards

aimed at ensuring transparency, accountability and investor protection. These standards are mandatory and primarily regulated by the Chilean Corporations Law (Law No. 18,046) and overseen by the CMF.

Publicly traded shares must be registered with the CMF and listed on a stock exchange. Listed companies are under continuous CMF supervision and must comply with stringent reporting and disclosure obligations.

Key governance requirements include:

- **Board structure:** Listed corporations must have a board of at least five directors, versus three for closed corporations. Independence and oversight capacity are essential features of the board.
- **Disclosure obligations:** Companies must publish key corporate governance documents, including financial statements, shareholder meeting minutes, and policies, which must be accessible on their websites.
- **Annual reporting:** Companies must prepare and submit a detailed annual report covering financial results, governance practices, and strategic direction.
- **Operational restrictions:** Certain activities require regulatory pre-approval or are subject to sector-specific limitations to safeguard market integrity.

Although these requirements are mandatory for publicly traded entities, many private companies voluntarily adopt similar standards to build trust and attract capital.

Companies in regulated industries such as banking, insurance, and pensions face additional obligations under sector-specific laws and CMF oversight, reflecting the need for enhanced

data privacy, consumer protection and financial system stability.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Chile is advancing key developments in corporate governance, with a particular focus on ESG reporting, compliance, board diversity, and cybersecurity.

ESG and Sustainability Reporting

The CMF continues to expand ESG disclosure requirements. Under General Rule No. 461, publicly traded companies must report on climate-related risks in line with international standards, such as those from the TCFD. As a result, companies are expected to embed carbon neutrality goals, environmental risk management, and supply chain sustainability into their corporate governance frameworks.

White-Collar Crime and Environmental Accountability

The enactment of Law No. 21,595, fully effective since 2024, significantly reformed Law No. 20,393 on the criminal liability of legal entities. The updated framework broadens the scope of crimes attributable to companies and their representatives, increases penalties, and emphasises environmental crimes and corporate responsibility in governance and compliance structures.

Gender Diversity on Boards

A bill entitled “*More Women on Boards*” has been approved by the Chamber of Deputies and is currently under discussion in the Senate. This bill proposes a suggested maximum quota of 60% for the gender with greater representation on company boards. The CMF will assess the adoption of this policy every four years, starting

from the sixth year after the law's enactment, using objective indicators to ensure that at least 80% of companies adopt the suggested quota and that less than 5% have no women on their boards.

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from the sixth year after the law's enactment, using objective indicators to ensure that at least 80% of companies adopt the suggested quota and that less than 5% have no women on their boards.

Cybersecurity and Data Protection

Boards are increasingly expected to address cybersecurity and data protection governance, as digital threats to the financial and corporate sectors intensify. Chile enacted Law No. 21.719, a new Personal Data Protection Law aligning with international standards (like the GDPR). It establishes a Personal Data Protection Agency, expands individual rights (eg, access, deletion, portability), mandates data protection officers, and requires breach notifications. It comes into force on 1 December 2026. Under Law No. 21.663, in effect since 1 January 2025, Chile created the National Cybersecurity Agency (ANCI) and established strict obligations for critical infrastructure operators (OVIs), including mandatory reporting and implementation of cybersecurity management systems.

Greenwashing Regulation

A bill to prevent and punish greenwashing is currently under discussion in the Chamber of Deputies. The proposed legislation mandates that companies advertising their products or services with a focus on sustainability must provide complete, truthful, verifiable and accurate information. Failure to do so would result in penalties.

Additionally, practices carried out merely in compliance with legal and regulatory provisions or mitigation, repair, compensation or voluntary commitments may not be advertised as sustainable.

2.2 ESG Considerations

In Chile, ESG reporting requirements have become more robust, particularly for publicly listed companies, following the issuance of General Rule No. 461 by the CMF. This regulation requires that ESG-related disclosures be integrated into the Annual Report (*Memoria Anual*).

Key ESG reporting components include:

Corporate Governance Practices

Companies must disclose how they evaluate and ensure compliance with internal governance practices, highlighting mechanisms for transparency, board composition, executive compensation and internal control systems.

Environmental Sustainability

Disclosures must address environmental risk management strategies, climate-related risks and opportunities, carbon neutrality goals and sustainability practices along the supply chain. These align with TCFD recommendations and international best practices.

Social and Human Rights Policies

The report must detail how the company addresses social impact, labour practices, community engagement and respect for human rights within its operations and business relationships.

Conflict of Interest Policies

Entities must explain how they identify and manage potential conflicts of interest across their operations, particularly in decision-making processes.

Research and Development

Companies are required to disclose their investments in innovation and technology, showcasing

ing their commitment to long-term value creation and competitiveness.

Diversity and Inclusion

ESG disclosures must include the company's diversity and inclusion policies, gender representation on boards and in management, and actions taken to promote inclusive workplace practices.

CMF's General Rule No. 461 requires companies to align their ESG disclosures with the Sustainability Accounting Standards Board (SASB) standards. These are industry-specific, identifying sustainability-related issues most relevant to investor decision-making across 77 industries. Each standard includes disclosure topics and associated metrics tailored to the specific sustainability risks and opportunities of that industry.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

In Chile, corporate governance and management are typically structured around three core bodies, each with distinct responsibilities to ensure effective oversight and operational control.

Shareholders' Meeting

This is the highest decision-making authority within a company. Shareholders vote on key corporate matters, such as the appointment or removal of board members, approval of financial statements, profit distribution, mergers or spin-offs, and amendments to the company's by-laws.

Board of Directors

The board is responsible for setting the company's strategic direction, supervising executive management and overseeing the company's general performance and compliance with legal obligations. Listed corporations are required to have a minimum of five board members, while closed corporations need only three.

Notably, under Law No. 18,046, certain publicly listed companies are mandated to form a Directors' Committee (*Comité de Directores*) with most independent directors. This requirement only applies to companies that meet specific criteria.

Executive Management

Led by the Chief Executive Officer (CEO) or General Manager (*Gerente General*), this team is tasked with the day-to-day management of the company. They implement the strategies defined by the board and ensure operational efficiency.

In addition to these core bodies, companies, especially those with publicly traded shares - may establish specialised committees, such as audit and risk and human resources.

3.2 Decisions Made by Particular Bodies

In Chile, corporate decision-making is structured under a defined hierarchy, with specific powers and responsibilities reserved to each governing body. The primary decision-making bodies operate as follows.

Shareholders' Meeting

As the supreme corporate body, the Shareholders' Meeting is responsible for the most critical decisions affecting the company's structure and overall direction. Matters exclusively reserved to this body include:

- Corporate structure and governance: Approval of by-law amendments, capital increases or reductions, mergers, spin-offs, transformations, and company dissolution.
- Financial matters: Approval of annual financial statements, the annual report (*memoria anual*), and appointment external auditors.
- Board composition and compensation: Appointment or removal of board members and determination of their remuneration.
- Profit distribution: Approval of dividend distribution, including setting minimum mandatory dividends as established by law or by-laws.

These decisions generally require qualified quorums depending on the nature of the resolution (eg, extraordinary versus ordinary shareholders' meetings).

Board of Directors

The board is tasked with the strategic and supervisory role over corporate affairs. Key powers include:

- proposing matters to be submitted to the shareholders' meeting;
- reviewing financial statements and proposing dividend distribution;
- appointing and removing the general manager (CEO) and, in some cases, other top executives;
- approving interim dividends, for which directors are personally liable if paid based on inaccurate data; and
- defining the company's business strategy, approving internal policies, and overseeing compliance and risk management.

Certain decisions - such as appointing executives, approving internal control systems, and defining general operational guidelines - fall strictly within the board's remit.

Executive Management

Led by the general manager (CEO), executive management is responsible for the daily operation and execution of the business strategy set by the board. Key decisions and responsibilities include:

- implementing corporate strategy and managing the company's commercial and administrative activities;
- hiring and managing personnel, negotiating contracts, and dealing with suppliers and clients, all within the limits set by the board; and
- reporting to the board on performance, operational risks, and compliance matters.

While executive management enjoys autonomy in day-to-day decisions, it must act within the strategic framework defined by the board and cannot unilaterally undertake actions reserved to the board or shareholders' meeting.

3.3 Decision-Making Processes

The process for decision-making in Chilean companies varies depending on the corporate body.

Executive Management

Executive management operates under internal delegation and guidelines established by the board of directors. Decision-making is typically carried out informally and continuously, in accordance with the company's internal policies and governance structure. The general manager (CEO) and other executives make decisions autonomously within their designated authority, without requiring formal sessions or resolutions, except where board approval is expressly required by law or the by-laws.

Board of Directors

The board of directors must meet formally to deliberate and resolve corporate matters. The process includes:

- Convening meetings in accordance with the company's by-laws or board regulations, usually monthly or as needed.
- Quorum requirements: Most directors must be present to constitute a valid quorum.
- Decision-making: Resolutions are adopted by the majority vote of those present, unless the by-laws or law require a higher quorum for specific matters.
- Record-keeping: All resolutions must be recorded in official board meeting minutes, signed by all attending directors and maintained in a formal minute book.

Shareholders' Meeting

Shareholders make decisions in duly convened ordinary or extraordinary meetings, depending on the nature of the matters to be resolved. The process is as follows:

- Notice of meeting: Must be issued in accordance with legal and by-law requirements, typically through three publications in the Official Gazette.
- Quorum: The required quorum varies depending on the type of meeting and the matters to be discussed. Extraordinary meetings and certain resolutions (eg, mergers) require higher quorum thresholds.
- Voting: Resolutions are adopted by the majority of shares present or represented, subject to any special voting thresholds under Law No. 18,046 (*Ley sobre Sociedades Anónimas*) or the company's by-laws.
- Documentation: Decisions must be recorded in the shareholders' meeting minutes, signed

by the chair and secretary of the meeting, and often notarised or registered.

4. Directors and Officers

4.1 Board Structure

The structure of board of directors in Chile is governed by the Law on Corporations (Law No. 18,046) and varies depending on whether the company is publicly or privately held.

Composition

- Listed corporations (*Sociedades Anónimas Abiertas*) must have at least five directors.
- Closed corporations (*Sociedades Anónimas Cerradas*) require a minimum of three directors, unless the bylaws provide otherwise.

Term and Re-election

Directors may serve for a maximum three-year term, after which they may be re-elected indefinitely. The term begins at their election by the shareholders' meeting and ends once their successors are appointed.

Election Process

Directors are elected by the shareholders' meeting using a cumulative voting system, where each shareholder may distribute their votes among one or more candidates, based on the number of shares held. This system allows minority shareholders to concentrate votes and potentially elect a representative.

Chairman of the Board

Once constituted, the board elects a Chairman (*Presidente del Directorio*) from among its members by a majority vote. The chairman represents the board and presides over its meetings.

Independent Directors

Publicly traded companies meeting certain thresholds - such as having high market capitalisation or dispersed ownership - are required to appoint independent directors, as defined by law and CMF regulations.

Board Committees

Some companies are required by law to establish a directors' committee (*Comité de Directores*) - especially when they have significant asset size or a large shareholder base. This committee must be led by an independent director and is responsible for overseeing internal controls, related-party transactions, and external audits.

In addition, many corporations voluntarily establish other specialised committees (eg, audit & risk and human resources).

These bodies support the board by providing deeper oversight into complex areas and are considered good governance practice.

4.2 Roles of Board Members

The roles of board members in Chile are defined primarily by the Law on Corporations (Law No. 18,046) and the corporate governance standards issued by the CMF. The board is collectively responsible for the strategic oversight and governance of the company, while individual members may hold specific functions.

Chairman of the Board (*Presidente del Directorio*)

Elected by most of the board, the chairman:

- leads board meetings, ensuring orderly deliberation and timely decision-making;
- co-ordinates the board's work and serves as a liaison between the board and executive management; and

- represents the board, including before regulators and in shareholder meetings.

Directors (General Members)

All directors, whether independent or not, share core responsibilities. These include:

- participating in strategic planning and approving key corporate policies;
- overseeing financial performance, including reviewing and approving financial statements;
- supervising risk management and internal controls;
- fulfilling fiduciary duties of loyalty and diligence, acting in the best interests of the company and all shareholders; and
- ensuring compliance with legal, regulatory and ethical standards.

Independent Directors

Under specific conditions (eg, market capitalisation, ownership dispersion, or certain related party transactions) publicly traded companies must appoint independent directors as defined by Law No. 18,046 and CMF rules.

These directors:

- enhance objectivity and independence in board discussions;
- mitigate conflicts of interest, particularly in transactions with related parties; and
- often chair or participate in the Directors' Committee, which has specific legal duties in oversight and audit review.

Board Committees

Companies, particularly large or listed entities, may establish specialised committees, either by law or voluntarily. The Directors' Committee (mandatory under certain thresholds) must

include at least one independent director, and oversees:

- related-party transactions;
- external audit selection and review; and
- financial reporting integrity.

Other common committees include:

- The Audit and Risk Committee;
- Human Resources Committee; and
- Corporate Governance or Sustainability Committee.

4.3 Board Composition Requirements/Recommendations

Under Chilean corporate law (Law No. 18,046), board composition is subject to the following formal requirements:

- Directors must be natural persons, not legal entities.
- Publicly traded corporations must have at least five directors, while closely held corporations require a minimum of three (as outlined in **Section 4.1 Board Structure**).

Beyond these baseline legal requirements, there are no mandatory rules concerning the diversity, background, or independence of board members — except in a limited number of specific scenarios.

- Independent directors: Required under certain conditions for publicly traded companies, such as exceeding UF1.5 million (*Unidades de Fomento*) in equity or having a significant shareholder dispersion. These companies must also form a Directors' Committee, which must include at least one independent director.

- Gender diversity (in progress): As of 2025, Chile does not yet mandate gender quotas, but a bill currently under discussion in Congress seeks to introduce mandatory female representation on boards of listed companies. The bill proposes a 40% gender balance quota, with a phased implementation period. This aligns with growing international ESG standards and CMF's increasing focus on board diversity.
- CMF Recommendations: While not legally binding, the Financial Market Commission encourages companies to disclose voluntary policies regarding board diversity, including gender, age, nationality, and professional background, as part of their ESG reporting under General Rule No. 461.

In practice, many Chilean corporations are proactively addressing board diversity and independence as part of broader ESG and governance best practices, even in the absence of rigid legal mandates.

4.4 Appointment and Removal of Directors/Officers

The board of directors is appointed and removed as a whole by the company shareholders, during general shareholders meetings. If a director vacates their position before the expiration of their term, the board may appoint a temporary director to assume their position until the shareholders' meeting, where the board of directors must be renewed.

4.5 Rules/Requirements Concerning Independence of Directors

The independence of directors and regulation of conflicts of interest in Chile are primarily governed by the following legal frameworks:

- Law No. 18,046 on Corporations (LSA);

- Law No. 18,045 on the LMV;
- CMF General Rule No. 533, on independent directors and the policy for electing directors for subsidiary companies;
- Decree Law No. 211 of 1973 (Free Competition Law or LPLC).

Under these frameworks directors must act in the best interests of the company, rather than in pursuit of personal or third-party interests. They are bound by fiduciary duties, including duties of loyalty, diligence and disclosure.

Certain publicly traded companies are required to appoint at least one independent director when they exceed UF1.5 million in equity or have significant shareholder dispersion. These directors must meet strict independence criteria, including:

- no recent employment ties to the company or its affiliates;
- no close family or business ties with major shareholders or executives;
- not holding significant share ownership in the company.

These companies must also establish a Directors' Committee, which must include at least one independent director. This committee oversees internal controls, risk management, related-party transactions, and executive compensation.

Directors are required to disclose any personal, familial, or financial interests that might compromise their independence or lead to conflicts of interest. Additionally, related-party transactions must be thoroughly reviewed and approved by the board in accordance with established procedures.

The interested director must:

- disclose their interest to the board;
- abstain from voting on the transaction;
- ensure the transaction is submitted to the shareholders for ratification in certain cases (eg, if material or not carried out at arm's length).

LPLC interlocking prohibits individuals from serving simultaneously as directors or executives of competing companies when each company (or its business group) has annual revenues exceeding UF100,000. This restriction is aimed at preventing anti-competitive coordination and collusion risks.

The National Economic Prosecutor's Office (FNE) has actively enforced this provision, and in 2025 the Competition Tribunal (TDLC) issued its first decision applying the interlocking prohibition, confirming its enforceability and establishing jurisprudence on its scope and application.

4.6 Legal Duties of Directors/Officers

In Chile, the main legal duties of directors and officers are established by the LSA and the LMV, as well as other relevant statutes such as the Criminal Liability of Legal Entities Law (Law No. 20,393).

The principal duties include:

Duty of Care (*Diligencia y Cuidado*)

Directors and officers must act with the diligence and care that a reasonably prudent person would exercise in similar circumstances. This includes being properly informed before making decisions, supervising corporate affairs, and participating actively in board and committee meetings.

Duty of Loyalty (*Lealtad*)

Directors must always act in the best interests of the company, not in their personal interest or on behalf of third parties. This fiduciary obligation includes:

- avoiding conflicts of interest;
- refraining from using their position for personal gain;
- not disclosing or using confidential company information improperly.

Duty of Information and Oversight

Directors and officers must:

- review and oversee the company's financial statements, internal controls, and risk management;
- ensure that adequate corporate governance and compliance frameworks are in place.

Duty of Transparency

Directors must ensure that the company complies with its disclosure obligations, including timely, accurate, and complete reporting to shareholders and regulators (such as the CMF), particularly with respect to:

- financial statements;
- material events (*hechos esenciales*);
- related party transactions.

Legal and Regulatory Compliance

Directors and officers are responsible for ensuring that the company:

- complies with tax, labour, environmental, and financial regulations;
- implements crime prevention models as required under Law No. 20,393, which may hold the company criminally liable for certain offences (eg, bribery, money laundering).

Personal Liability

Directors may be held personally liable for damages caused to the company, shareholders, or third parties if they breach their legal duties or act with gross negligence, wilful misconduct, or bad faith.

It is important to note that Chilean corporate law does not explicitly establish “*business judgment rule*” as found in some other jurisdictions. Consequently, directors do not have a formal legal presumption protecting their decisions made in good faith and with reasonable care. This means that directors’ actions may be scrutinised more strictly by courts or regulators, and they must be especially diligent in documenting and justify their decision-making processes to avoid liability.

4.7 Responsibility/Accountability of Directors

In Chile, directors owe their legal and fiduciary duties primarily to the company itself, as a separate legal entity. This principle is established under the LSA and reinforced by case law and regulatory guidance.

Key elements of this obligation include:

Duty to the Company (not to individual shareholders)

Directors must act in the best interests of the company, regardless of which shareholders appointed them or the ownership structure. They must act with the diligence and care of a good businessman.

Accountability to Shareholders as a Group

While the primary duty is owed to the company, directors are accountable to shareholders collectively, not individually. Directors may be held personally liable for damages caused to the

company or its shareholders due to wilful misconduct, gross negligence, or breaches of legal duties.

Stakeholder Considerations

Chilean law does not impose a formal requirement to consider stakeholders such as employees, creditors, or the environment in the discharge of directors’ duties. However, to the extent these factors impact the long-term interests of the company, they may be considered under the duty to protect the company’s sustainability and reputation.

4.8 Consequences and Enforcement of Breach of Directors’ Duties

In Chile, directors who breach their legal or fiduciary duties may face civil, administrative and criminal consequences, depending on the nature and severity of the breach. The enforcement mechanisms are grounded in the LSA, the LMV, and Law No. 20,393 on corporate criminal liability.

Civil Liability

Directors may be held personally liable for damages caused to the company, shareholders or third parties if they act with gross negligence, wilful misconduct or breach of fiduciary duties. Shareholders can initiate derivative lawsuits on behalf of the company to seek compensation.

Administrative Sanctions

The CMF has authority to:

- impose fines and penalties;
- disqualify directors from holding office; and
- suspend or restrict the company’s operations or trading of its securities.

These sanctions are typically applied in cases of non-compliance with disclosure obligations,

related-party transactions, or failure to implement adequate governance and risk controls.

Criminal Liability

Under Law No. 20,393, directors may face criminal prosecution for offences such as:

- bribery;
- money laundering;
- environmental crimes; and
- fraud or misrepresentation.

If found guilty, directors can face fines, imprisonment, and reputational damage. The Public Prosecutor (*Ministerio Público*) is responsible for criminal investigations and prosecutions.

ESG and Reporting Failures

With the rise of ESG regulations (eg, CMF Rule No. 461), failure to provide accurate or complete ESG disclosures can also lead to regulatory sanctions and potential shareholder litigation, especially if such omissions mislead investors or affect share value.

Enforcement Trends

Recent enforcement trends show increased scrutiny from the CMF and courts, particularly regarding:

- conflicts of interest;
- board independence;
- cybersecurity and data protection; and
- environmental accountability.

Directors are expected to document their decision-making processes thoroughly to mitigate liability risks, especially in the absence of a formal business judgment rule in Chilean law.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Breaches of directors' duties can be enforced by several parties, each within their respective jurisdictions.

Shareholders

Shareholders may bring derivative lawsuits on behalf of the company to seek compensation for damages caused by directors' negligence, fraud, or breaches of fiduciary duties.

Regulatory and Criminal Authorities

The CMF supervises compliance with corporate governance laws and regulations. It can investigate violations and impose administrative sanctions such as fines, suspensions, or other penalties.

In cases involving criminal liability, such as corporate fraud, bribery, environmental crimes, or other illegal activities, the Public Prosecutor of Chile (*Ministerio Público*) is responsible for investigating and prosecuting directors under Law No. 20,393 on criminal liability of legal entities and other applicable criminal statutes.

Consequences of Breach

Civil liability: Directors can be held liable for damages caused to the company or third parties, potentially resulting in compensation payments.

Administrative sanctions: The CMF can impose fines, prohibit directors from holding office, or suspend trading of the company's securities.

Criminal penalties: Directors may face fines, imprisonment, or other criminal penalties depending on the severity and nature of the offence, following public prosecution by the *Ministerio Público*.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The remuneration and fees payable to directors must be approved by the shareholders at the annual ordinary shareholders' meeting. This includes any fixed fees, attendance fees, or other benefits granted to directors. In contrast, the remuneration and benefits for senior executives and officers (such as the CEO and other top management) are typically determined and approved by the board of directors.

Compensation policies must adhere to applicable corporate governance best practices and align with market standards. Directors and senior executives are prohibited from approving their own compensation to avoid conflicts of interest. Any remuneration or benefits that create conflicts or are inconsistent with approved policies may be deemed unlawful.

Directors who approve unlawful or unauthorised compensation may be subject to personal liability, including fines and potential removal from office. The CMF oversees compliance with these rules and can impose administrative sanctions such as fines, penalties, or other corrective measures on both individuals and the company. Failure to comply with remuneration approval requirements may also expose the company to reputational damage and shareholder disputes.

4.11 Disclosure of Payments to Directors/Officers

Remuneration of directors must be approved by the shareholders in the annual ordinary shareholders' meeting.

Although shareholders' meetings are private, in publicly traded corporations, they must be informed to the CMF and may be subject to dis-

closure obligations, making them much more susceptible to public knowledge.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The relationship between a company and its shareholders is primarily governed by the LSA and, for publicly traded companies, by the LMV and related regulations issued by the CMF.

Shareholders are the owners of the company's equity and exercise their rights mainly through participation in shareholders' meetings. They are entitled to:

- vote on key matters such as the election of directors, approval of financial statements, profit distribution, mergers, and amendments to the by-laws;
- receive dividends, if declared; and
- access certain corporate information, including meeting minutes and audited financial statements.

Every corporation must maintain a shareholders' registry, which records the ownership of shares and related changes. This registry is private and managed by the company or a designated administrator (eg, a stock registry agency).

In the case of publicly traded companies, the CMF requires disclosure of:

- the identity of controlling or major shareholders (typically defined as those owning 10% or more of the shares or voting rights);
- certain changes in ownership thresholds.

However, full shareholder lists are not publicly available, except when required in specific regulatory filings, investigations, or judicial proceedings.

5.2 Role of Shareholders in Company Management

Under Chilean law, shareholders do not participate in the day-to-day management of a company, which is entrusted to the board of directors and executive officers. This separation of ownership and management is a fundamental principle of corporate governance in Chile.

However, shareholders have significant rights and influence through shareholders' meetings, where they may vote on key corporate matters, including:

- appointment and removal of directors;
- approval of the company's annual financial statements;
- distribution of dividends;
- major corporate actions such as mergers, spin-offs, or amendments to the by-laws;
- director and auditor compensation (in the case of directors, mandatory for publicly traded companies).

While shareholders cannot issue binding instructions to the board or management regarding operational matters, they may challenge decisions that infringe upon their rights or breach corporate governance principles. In some cases, shareholders can bring legal actions (eg, nullity or liability claims) or request the intervention of the CMF if public market rules are violated.

5.3 Shareholder Meetings

Shareholder meetings are required under the *Ley sobre Sociedades Anónimas* (LSA). The LSA distinguishes between ordinary and extraordinary shareholders' meetings, each governed by specific rules.

Ordinary Shareholders' Meetings

Corporations must hold an ordinary shareholders' meeting annually, within the first four months of each year, to address the following matters:

- reviewal of the company's general situation, including the reports of account inspectors and external auditors, and the approval of the annual report, balance sheet, and other financial statements presented by management;
- the distribution of profits;
- the appointment or removal of board members and external auditors.

Extraordinary Shareholders' Meetings

These must be convened for matters not covered in ordinary meetings, particularly those that may involve amendments to the company's by-laws. Examples include:

- capital increases or reductions;
- mergers, spin-offs, or dissolutions;
- changes to the company's corporate purpose; and
- other matters that, by law or by-laws, require an extraordinary meeting.

Quorum and Approval Requirements

A valid meeting requires a legal call (citation) and the presence (in person or by proxy) of shareholders representing at least 50%+1 of the issued voting shares. Resolutions at ordinary meetings are adopted by majority vote of the shares present or represented. Extraordinary meetings may require higher quorums and vot-

ing thresholds, depending on the nature of the decision.

Meetings must comply with notice periods and formalities established in the company's by-laws and the LSA, including the method and timing of the call. Failure to follow these requirements may invalidate resolutions and expose directors or officers to liability or regulatory sanctions.

5.4 Shareholder Claims

Under the LSA and the LMV, shareholders may pursue civil, administrative, or even criminal remedies against the company, its directors, or controlling shareholders in cases of misconduct or breaches of legal duties.

The principal bases of claim available to shareholders include:

- breach of fiduciary duties by directors, such as acting in self-interest, engaging in negligent management, or failing to act with due diligence and care;
- abuse of controlling position or majority rights, where controlling shareholders exercises their influence in a manner that harms minority shareholders or the company itself;
- violation of shareholders' rights, such as the right to receive dividends, access corporate information, or participate in decision-making processes;
- contraventions of market conduct or disclosure obligations, including insider trading or market manipulation, which may give rise to administrative sanctions by the *Comisión para el Mercado Financiero* (CMF) or criminal charges by the *Ministerio Público*.

In addition, dissenting shareholders have appraisal rights (*derecho a retiro*) in certain fundamental corporate decisions - such as mergers,

transformations, or the sale of substantial assets - enabling them to request that the company repurchase their shares at fair market value.

Shareholders can bring individual or derivative actions depending on whether the harm is personal or affects the company. Directors may be held personally liable if their actions breach statutory or fiduciary duties, subject to standards of wilful or negligent conduct.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Shareholders of publicly traded companies in Chile are subject to several disclosure obligations under the LMV and regulations issued by the CMF:

Threshold Disclosures

Shareholders who acquire a 10% or greater interest in a publicly traded company must notify the CMF. Any subsequent increase or decrease of 5% or more in their holdings must also be disclosed. These reports must include information about the purpose of the acquisition, sources of funding, and any plans to acquire control of the company.

Disclosure of Control intentions

Individuals or entities seeking to gain control of a company - whether through a public tender offer (OPA) or otherwise - must disclose their intentions to the CMF and the market. This includes reporting coordinated actions among shareholders that may affect control or governance.

Ultimate Beneficial Ownership (UBO)

Although publicly traded companies are not currently required to disclose a full list of all shareholders, regulations enforced by the CMF and the UAF require companies - especially financial institutions and entities subject to AML/CTF

regulations - to identify and report their ultimate beneficial owners.

Institutional Investors and Stewardship

Institutional investors such as pension funds (AFPs) must follow investment regulations issued by the *Superintendencia de Pensiones* and may be subject to additional reporting requirements on their voting behaviour and stewardship policies, ensuring alignment with responsible investment practices.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

In Chile, companies are subject to annual and periodic financial reporting requirements that vary depending on whether they are publicly traded or closely held, as regulated primarily by the LSA, the LMV, and applicable regulations issued by the CMF. These reports must comply with International Financial Reporting Standards (IFRS).

Annual Financial Reporting

Publicly traded companies must submit their audited annual financial statements to the CMF within 90 days following the end of the fiscal year. These must include the balance sheet, income statement, cash flow statement, statement of changes in equity, and explanatory notes, along with the report of the external auditor.

Quarterly Reporting

Issuers must also submit unaudited quarterly financial statements within 60 days following the end of each quarter. These updates allow the market and regulators to monitor the company's financial position, performance, and material changes.

Integrated Reporting and ESG Disclosures

Under Norma de Carácter General (NCG) No. 461, publicly traded companies are required to include disclosures on corporate governance, climate-related risks, and sustainability practices as part of their annual reporting. These ESG disclosures are aligned with international standards and seek to promote transparency on non-financial risks.

Sector-Specific Reporting

Companies operating in regulated sectors - such as banks, insurance companies, and pension fund administrators - must also comply with industry-specific reporting obligations, including periodic risk assessments, capital adequacy reports, and liquidity metrics, as established by the respective regulators and CMF rules.

Closed corporations are not subject to public reporting requirements before the CMF. However, they must prepare and submit their annual financial statements and reports for approval by the ordinary shareholders' meeting, which must be held within the first four months of the year (ie, by 30 April).

6.2 Disclosure of Corporate Governance Arrangements

In Chile, publicly traded companies are required to disclose their corporate governance arrangements through their annual reports, sustainability disclosures, and other regulatory filings, primarily under the supervision of the CMF.

Annual Corporate Governance Disclosure

Public companies must include in their annual report (*Memoria Anual*) detailed information on:

- board composition and structure;
- board committees and their functions;
- executive compensation policies;

- internal control and risk management systems;
- compliance and ethics programmes;
- sustainability and ESG practices, pursuant to CMF Rule No. 461.

By-laws and Corporate Policies

Companies must also make publicly available - typically via their corporate websites - key governance documents such as:

- company by-laws (*estatutos sociales*);
- codes of ethics and conduct;
- corporate governance manuals or frameworks.

Sector-specific Governance Requirements

Companies in regulated sectors such as banking, insurance, and pension fund administration are subject to stricter governance and disclosure standards, including periodic filings on risk oversight, capital requirements, and regulatory compliance.

Ongoing Compliance and Monitoring

The CMF frequently updates its governance and disclosure regulations. As such, companies must continuously monitor regulatory changes to maintain compliance and avoid administrative sanctions.

While closely held corporations (*sociedades anónimas cerradas*) are not required to make these disclosures publicly, they may still voluntarily adopt governance frameworks aligned with best practices, especially when dealing with institutional investors or preparing for public listing.

6.3 Companies Registry Filings

In Chile, the incorporation and registration of companies involve multiple steps before differ-

ent bodies, primarily the Commerce Registry (*Registro de Comercio*) of the company's domicile and, in some cases, the Internal Revenue Service (*Servicio de Impuestos Internos*, or SII) and the CMF for regulated or publicly traded entities.

Registration and Publication Requirements

The company must be formed by public deed (*escritura pública*) or, in certain cases, through the online platform *Registro de Empresas y Sociedades* (RES) administered by the Ministry of Economy.

An abstract (*abstracto*) of the public deed must be:

- registered in the Commerce Registry (*Registro de Comercio*) corresponding to the company's domicile; and
- published in the Official Gazette (*Diario Oficial*) within 60 days of the company's incorporation.

Supervisory Role of the Commerce Registry

The Commerce Registry reviews the abstract for formal errors before registration.

If the required filings are not registered or published timely, the incorporation or corporate modification has no legal effect and is considered null and void under Chilean law.

Public Availability of Records

Once registered, the abstract becomes part of the public Commerce Registry.

Anyone may request copies or certificates from the Registry for a fee.

Likewise, the original public deed is held by the notary public who authorised it, and archived

in the judicial archive, also accessible upon request.

Online Incorporation

Companies may alternatively be created through the *Registro de Empresas y Sociedades* (www.tuempresaenundia.c).

This system allows standardised electronic by-laws and immediate registration and tax ID assignment (RUT).

While faster, the RES system is only available for companies using pre-approved templates and lacks notarial oversight.

Additional Filings

All companies must register with the SII to obtain a tax ID (RUT) and begin operations.

Publicly traded companies must also register with the CMF, which monitors their corporate structure, financial reporting, and governance practices.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

In Chile, publicly traded companies - including listed corporations, financial institutions, and other regulated entities - are required to appoint an external auditor to review and certify their financial statements during the annual ordinary shareholders meeting.

The appointment and relationship between the company and the external auditor are subject to the following key requirements:

Independence of the Auditor

The external auditor must be independent from the company, with no financial, business, or personal relationships that could impair its objectivity and impartiality.

Registration and Compliance

The auditor must be registered with the CMF and perform audits in accordance with IFRS and auditing standards recognised in Chile.

Scope of Work

The auditor is responsible for a thorough review of the company's financial statements, verifying regulatory compliance, assessing internal controls and risk management systems, and detecting any irregularities or mistakes.

Audit Report and Disclosure

Upon completion, the auditor issues an independent audit report detailing their findings and certifying the accuracy and fairness of the financial statements. This report must be approved by the company's board of directors and shareholders and subsequently filed with the CMF.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

In Chile, directors have specific responsibilities regarding risk management and internal controls, particularly in publicly traded companies. The key requirements include:

Fiduciary Responsibility

Law No. 18,046 establishes that directors must act in good faith and in the best interest of the corporation. Directors have a duty of care and duty of loyalty, meaning they must ensure the corporation operates ethically, responsibly, and transparently. They must avoid conflicts of interest and prioritise shareholder interests, ensur-

ing risk management policies prevent financial harm.

Risk Oversight and Compliance

Directors are responsible for identifying, evaluating, and mitigating risks that may affect the company. To this end, they must implement effective internal controls and ensure compliance with financial and operational regulations. Publicly traded companies are required to establish risk management frameworks, including cybersecurity and financial risk assessments.

CMF Compliance

Law No. 18,045 imposes strict reporting requirements on publicly traded companies, and directors must ensure financial transparency. Directors oversee internal audits and verify compliance with accounting standards.

Liability and Accountability

Directors may be held personally liable for mismanagement of risks or failure to uphold fiduciary duties. Negligence leading to financial harm or regulatory breaches can result in legal consequences, including fines or removal from the board.

Transparency and ESG Considerations

Under newer regulations, directors must ensure companies disclose risk management practices and internal control measures in their annual reports. Additionally, directors in specific sectors such as banking, insurance, and social security face stricter regulatory requirements.

Trends and Developments

Contributed by:

Juan Pablo Halpern, Arturo Pino, Francisca Zuccone and Carolina Schiele
Clyde & Co Chile

Clyde & Co Chile is the Santiago office of Clyde & Co, a dynamic international law firm with over 2,400 lawyers and 3,200 legal professionals operating from over 60+ offices and associated offices in six continents. It focuses on providing a complete legal service to businesses and governments around the world in its core sectors of insurance, construction, transport, energy, infrastructure and trade and commodities. Its globally integrated teams provide a com-

prehensive range of legal services and advice to businesses operating at the heart of global trade and commerce. The multidisciplinary team brings together a dedicated group of experienced professionals, with expertise across diverse practice areas, and has a robust understanding of the regulatory and policy drivers of the market, and extensive experience through a wide range of sectors, contexts, in solving problems and providing practical solutions.

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CHILE TRENDS AND DEVELOPMENTS

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CHILE

Chile's Progressive Push for Sustainability, Greenwashing Regulation, and Gender Diversity in Corporate Leadership

Various institutions and market participants have adopted measures to mitigate the impact of business activities within the framework of sustainability strategies (ESG). In this context, sustainability refers to the effective management and reduction of risks and impacts arising from corporate operations, taking into account environmental, social, and governance factors. Its ultimate objective is to generate long-term value - not only for partners and shareholders but for all stakeholders involved.

Against this backdrop, the aim is to provide a brief overview of recent developments in Chile's national sustainability landscape.

Chile has introduced new regulations and amended existing ones as part of its commitment to the United Nations 2030 Agenda for Sustainable Development. Further regulatory developments are expected to support the adoption of sustainability standards. Through this evolving legislative framework, Chile seeks to strengthen its commitment to sustainability and position itself as a credible actor aligned with global ESG trends.

In the sections that follow, local developments in sustainability, with a focus on recent and proposed legislation concerning sustainability reporting, greenwashing regulations, and the promotion of women's participation on corporate boards are examined.

Sustainability reporting

Chile has long required open companies to publish annual reports, but has recently strengthened regulations mandating broader disclosures on sustainability issues, as detailed below.

Currently, open companies and securities issuers - as well as certain special legal entities - are required to publish annual reports in accordance with General Rule No. 461 of 2021, which amended General Rule No. 30 of 1989, both issued by the Financial Market Commission (CMF).

Annual reports must include information such as ownership, controllers, corporate governance structure, board operations, key executives, business models, assets, and overall strategy, among other key details. Additionally, companies are required to disclose sustainability-related information, such as their "*mission*" and "*vision*", risk management approach, stakeholder relationships, labour, and gender policies, and whether they have whistle-blower channels, among other aspects.

However, at the end of 2024, General Rule No. 519 amended the existing regulation to expand the scope of sustainability reporting, particularly regarding adherence to international standards and gender equality.

From now on, companies must report on their adherence to international principles and criteria, including corporate governance practices (such as the S&P Dow Jones policies, the Global Reporting Initiative Standard (GRI), or the OECD Principles of Corporate Governance). Additionally, they must disclose sustainability-related information based on metrics developed by the Sustainability Accounting Standards Board (SASB) and indicate whether they have an independent sustainability verification system, which could be fulfilled through certifications (such as ISO, BCorp, Zero Waste, or others).

In the same spirit, the new rule also mandates disclosure of the company's risk management

guidelines, specifying whether they align with international criteria. Examples of such criteria include the recommendations of the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the Control Objectives for Information and Related Technology (COBIT), and the standards set by the International Organization for Standardization (ISO).

Also, under the new rule, companies must report on their IFRS Section 1 and IFRS Section 2 financial and climate-related sustainability information, in compliance with the International Sustainability Standards Board (ISSB) of the IFRS Foundation.

Regarding gender equality, the regulations now mandate reporting on the company's personnel by sex, distinguishing the number of employees working regular or part-time hours, specifying whether they are working remotely, and identifying any special work arrangements for employees responsible for caring for children under 12 years old or carrying other family obligations.

Additionally, companies must now report on the procedure for electing their board of directors, regarding gender issues. Specifically, they must disclose whether the process ensures diversity among nominees, including whether it requires that no more than 60% of the candidates on the list belong to the same sex.

Companies must also report on the implementation of sexual harassment prevention training and disclose the number of complaints received, specifying the sex of the complainant.

Finally, regarding sanctions for non-compliance with annual report publication requirements - including the latest requirements mentioned above - it is worth noting that at the end of

2023, Law No. 21,595 on Economic Crimes was enacted. This law introduced criminal penalties for directors, managers, or main executives who improperly disclose company information on their annual reports, with punishments ranging from medium to maximum degrees of minor imprisonment, equivalent to 541 days to five years.

As noted, Chile has significantly strengthened its sustainability regulations, implementing more rigorous requirements for companies to enhance transparency, accountability, and adherence to international standards.

These measures reflect Chile's commitment to fostering a more sustainable corporate landscape, aligning with global Environmental, Social, and Governance (ESG) trends. By integrating sustainability into corporate governance, Chile positions itself as a forward-thinking market, not only keeping pace with leading economies but also enhancing its appeal to institutional investors who increasingly prioritise ESG-conscious business practices.

In recent years, investors have seen a notable shift, favouring companies that demonstrate strong sustainability credentials, as they recognise the long-term value of responsible corporate conduct. In line with the above, sustainability-driven investment is no longer just an ethical or reputational concern; it has become a strategic advantage.

By implementing these measures, Chile enhances its position in the global economy, ensuring that its businesses remain attractive to investors seeking stable and responsible investment opportunities.

Greenwashing bill

Chile is currently debating a bill aimed at regulating greenwashing (*"the greenwashing bill"*). Until it is enacted, Consumer Law No. 19,046 on misleading advertising remains in force. The bill seeks, among other objectives, to define greenwashing and introduce measures to penalise those who fail to comply with the regulations.

Within the framework of ESG sustainability strategies, numerous institutions and market actors have implemented initiatives to reduce the environmental impact of business activities. These measures range from adopting cleaner production methods to promoting circular economy principles. However, alongside these genuine sustainability efforts, a paradox has emerged: greenwashing, a deceptive practice that distorts the true intent of environmental responsibility, leading to a false perception of corporate commitment to sustainability.

Greenwashing can be defined as a commercial strategy in which companies falsely claim, exaggerate or create misleading impressions about the environmental benefits of their products, services or operations. This practice often manifests in marketing campaigns, branding efforts and product labelling, where terms such as *"eco-friendly," "biodegradable,"* and *"100% natural"* are prominently displayed without adequate substantiation.

These practices not only mislead consumers and the market, but also slow progress toward sustainability by allowing companies to benefit reputationally without making meaningful environmental improvements.

In Chile, a bill to regulate greenwashing is currently being discussed. For the time being, Con-

sumer Law No. 19,046 on misleading advertising remains applicable.

As for the bill, its objective is, among other aspects, to define the concept of greenwashing and establish tools to sanction those who violate the regulation.

If approved, the bill will require companies to provide information in their advertising that is not only truthful and not misleading but also verifiable, establishing the obligation to maintain permanent and updated information on their websites regarding their environmental practices in the country, as well as in other countries where they operate or invest.

A novelty in the regulation is linked to the burden of proof at trial, as the bill alters the traditional rule on this. Thus, instead of the burden of proof falling on the complainant, the bill establishes that companies must prove the veracity of their statements in the challenged advertisement.

In terms of penalties, the bill establishes fines of up to 9,000 *Unidad Tributaria Mensual* or 'UTM', (approximately USD640,000) and a ban on any kind of advertising for a period of one to five years.

The court may also order the offender to carry out the necessary corrective publicity to amend the errors or falsehoods in the challenged publication. Additionally, the verdicts will be published in the National Environmental Information System (SINIA).

Furthermore, the bill intends to sanction the media that broadcast advertising classified as greenwashing, establishing fines equivalent to twice the economic benefit gained by such publication.

In addition, the bill will prohibit companies convicted of environmental damage or sanctioned by the Superintendence of the Environment from advertising on sustainability-related issues. The same will apply to companies whose partners, shareholders, directors, or managers have been convicted, among other offences, for anti-union practices or violations of fundamental workers' rights.

This initiative aligns with the standards set by the European Union, which has already enacted regulations to address greenwashing. In contrast, other countries in Latin American - such as Mexico, Brazil, Argentina, and Colombia - have yet to implement specific legislation targeting greenwashing. These countries primarily address these claims through their consumer protection laws.

If approved, Chile's bill would position the country as a regional leader in sustainability governance, establishing a dedicated legal framework to combat greenwashing as part of broader climate action efforts, ensuring stronger accountability and transparency to consumers and the market.

In this way, the country aims to demonstrate its commitment to sustainability and position itself as a player capable of adhering to the ESG principles that are currently setting the standard in the global market.

Bill to increase the presence of women on boards of directors

In 2022, a legislative proposal was introduced with the aim of establishing mandatory minimum quotas for women's representation on the boards of directors of specific private organisations. This initiative was designed as a concrete step toward achieving gender equality, recognis-

ing the need for greater female participation in senior leadership roles within private companies.

The gender quota bill is set against the backdrop of persistently low female participation in senior management positions, a challenge that spans across all industries. In this regard, Chile falls below the average of OECD countries in terms of women's representation in leadership roles, highlighting the need for systemic change.

In this scenario, said project was inspired by successful policies implemented in various European countries, including Iceland, France and Norway, where similar gender quotas have significantly increased women's presence in executive positions. By following these international examples, the proposed legislation seeks fostering more inclusive and diverse corporate governance.

This approach seeks to adopt gender diversity in corporate leadership, promoting more inclusive decision-making while holding organisations accountable for their progress in achieving equitable representation.

In this sense, the gender quota bill recognises that organisations with more women in executive positions often achieve stronger financial performance, adopt a more inclusive and dynamic workforce, enhance their ability to navigate challenges, and are better positioned to attract new business opportunities.

If enacted, the law will establish minimum quotas for women's representation on the boards of publicly traded companies - those listed on the stock exchange - as well as special stock companies, such as banks and insurance firms. This initiative aligns with the gender equality reporting requirements introduced in 2024 by the Finan-

cial Market Commission (CMF), which mandate transparency in corporate diversity efforts. It also underscores the country's commitment to implementing sustainable governance standards.

The implementation of these quotas will follow a gradual approach. In the first three years, a recommended benchmark of at least 20% female board participation will be encouraged. Between years three and five, this recommendation will increase to a minimum of 40%. While adoption of these quotas will remain optional during the initial five-year period, companies choosing not to comply must provide an explanation to the CMF, adhering to the “*comply or explain*” principle.

Beginning in the sixth year following the law's enactment, if approved, company boards will be required to maintain a minimum of 40% female representation. The same phased approach will also apply to the selection of alternate directors, ensuring sustained gender diversity in leadership positions.

If the election process for board members - outlined in the company's bylaws - fails to meet the required quota, the gender quota bill mandates that the election be repeated until the minimum percentage is reached. As a final measure, if compliance is still not achieved, the CMF may intervene and impose sanctions on the company, reinforcing the law's commitment to equitable representation.

The gender quota bill remains under review; however, it has recently made progress and is now undergoing its second constitutional examination.

By promoting gender diversity at the highest levels of corporate governance, the gender quota bill seeks to create a more equitable and forward-thinking business environment, reinforcing the value of diverse perspectives in strategic decision-making and long-term organisational success.

CHINA

Law and Practice

Contributed by:

Kevin Wang

Global Law Office

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Global Law Office (GLO) was one of the first leading law firms in the PRC to take an international perspective on its business, fully embracing the outside world. With more than 600 lawyers practising in the Beijing, Shanghai, Shenzhen and Chengdu offices, the firm continues to set the pace as one of the most innovative and progressive legal practices in China. Over the last 40 years, GLO has helped set the agenda for change through precedents, includ-

ing working on the first foreign general offer targeting Chinese companies on the Hong Kong Stock Exchange, the first state-owned red chip company listed in Hong Kong acquiring the controlling interest in an A-share company listed in China by means of a reverse takeover, and the first reverse merger case in which a red chip Hong Kong-listed public company spun off part of its China business to list on a share market.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

There are three principal forms of corporate/business organisation in China:

- companies;
- partnership enterprises; and
- individual proprietorship enterprises.

Only companies have the status of legal persons, and shareholders shall bear liabilities for a company to the extent of their respective subscribed capital contribution/shares. However, a shareholder who abuses the independent legal person status of the company or the shareholder's limited liabilities to evade debts, thereby prejudicing the interests of creditors of the company, shall be jointly and severally liable for the debts of the company.

Companies are categorised as limited liability companies and joint stock limited companies. Joint stock limited companies whose shares are listed and traded on a stock exchange are publicly traded companies.

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance requirements for companies are the Company Law of the People's Republic of China (the "Company Law") and five judicial interpretations of the Company Law. In addition to the laws, judicial interpretations and regulations, the activities of a company and all participants (including shareholders, directors, supervisors and officers) are governed by the articles of association of the company.

Publicly Traded Companies

Provisions on the supervision and administration of publicly traded companies are numerous and complex. As publicly traded companies are a type of joint stock limited company, the provisions of Chapter 5 of the Company Law, regarding joint stock limited companies, apply to them, and particularly, they are also subject to the special provisions of Section 5 of Chapter 5 regarding the organisation of publicly traded companies. The organisation and activities of publicly traded companies are also regulated by the Securities Law of the People's Republic of China, the regulatory rules of the China Securities Regulatory Commission (CSRC) and the relevant stock exchanges.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Corporate governance requirements for companies with publicly traded shares mainly include the following:

- the company shall establish and maintain effective mechanisms of shareholder meetings, boards of directors, boards of supervisors, independent directors, board secretaries and special committees in accordance with the law;
- the company shall be encouraged to appoint officers in an open and transparent manner;
- the company shall establish fair and transparent standards and procedures for evaluating the performance of directors, supervisors and officers;
- the company shall establish a mechanism linking remuneration with the company's performance and individual performance;
- the company shall be strictly independent from its controlling shareholder and actual control persons in terms of personnel, assets,

- financial affairs, organisational institutions, business, accounting and also their respective responsibilities and risks;
- decision-making procedures and information disclosure obligations shall be strictly performed in connection with related-party transactions in accordance with the relevant rules;
- the company shall establish and implement a management system of information disclosure – it shall make public disclosures on documents such as periodic reports, interim reports, prospectuses, offering prospectuses, listing announcements, acquisition reports, etc; and
- internal control and risk management shall be established.

Corporate governance requirements for companies with publicly traded shares are mainly stipulated in the Code of Corporate Governance of Publicly Traded Companies, which was issued by CSRC in 2018. Some requirements are mandatory, while others are voluntary. However, certain provisions seem to be voluntary, but in fact have become quasi-mandatory, because companies may be confronted with unnecessary complications if they have not strictly complied with them in the IPO procedure.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

The Company Law was revised on 29 December 2023, and the new rules came into effect on 1 July 2024, with the following hot topics in corporate governance arising:

- the reform of the registered capital system;
- the responsibility of the controlling shareholder and actual control person;
- the improvement of the legal representative system;
- the corporate governance structure about dual class equity;
- the competition between the centralism of the shareholders' meeting and the centralism of the board;
- the enrichment of shareholder derivative lawsuits;
- the protection of shareholders' rights; and
- the company autonomy and shareholder discretion in designing the company's articles of association.

The new revisions strengthen the protection of shareholders' rights and creditors' economic interests, improve the shareholder investment mechanisms, enhance compliance responsibility of corporate control persons and executives, and allow certain simplifications of the company governance structure.

The new Company Law specifically focuses on the issues arising from corporate control right competition, shareholder litigation and director responsibility. In addition, it defines the content scope of articles of association that can be agreed upon by shareholders. It still leaves gaps open on many practical issues and increases the need for professional advice and even legal battles for all relevant parties.

2.2 ESG Considerations

According to China regulatory rules, publicly traded companies shall disclose environmental information and fulfil social responsibilities such as poverty alleviation. ESG information disclosure is one of the obligations that publicly traded companies must fulfil, which requires them to incorporate “*environment*”, “*society*” and “*governance*” into the concept of enterprise development.

In 2024, China's stock exchanges issued more specific requirements on the sustainable development report for publicly traded companies. A combination of mandatory disclosure and voluntary disclosure should be adopted for ESG reports, and violations may cause regulatory or disciplinary actions.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

In China, the principal bodies involved in the governance and management of a company include the shareholder meeting, the board of directors, the board of supervisors and the manager.

- The shareholder meeting is the key organ of authority, responsible for making decisions on fundamental issues and electing the main members of the board of directors and the board of supervisors.
- The board of directors is the executive function in corporate governance. The managers are appointed by the board of directors and the managers' functions are defined in the articles of association. Depending on their relevant authorities in this executive function, directors or managers may hold the central position in the company's day-to-day decision-making process.
- The board of supervisors is the supervisory organ, responsible for supervising the execution of business and the company's financial status. Without the board of supervisors, the company may also set up an audit committee in the board of directors to exercise the same functions and powers, in which case the board of directors actually has the supervisory responsibilities.

In general, the new company law allows the removal of supervisors from the corporate governance structure. It may also, however, raise the concern of self-supervision by the board of directors itself, leaving an open question on how to balance the board's power in such structure.

3.2 Decisions Made by Particular Bodies Decisions of the Board of Directors

The board of directors shall decide on the following matters:

- determining the company's business plans and investment programmes;
- determining the establishment of the company's internal management departments;
- formulating the company's basic management system; and
- deciding on the hiring or dismissal of the managers and their remuneration.

The new Company Law deletes the board's function of formulating plans in respect of the company's annual budget and final accounts, which gives the company a discretion to transfer this function from the board of directors to the senior managers by an elaboration in its articles of association.

In addition, the board of directors shall exercise other powers prescribed by the articles of association and empowered by the shareholders' meeting.

Powers That the Shareholders' Meeting can Give to the Board of Directors

Based on the empowerment by the shareholders' meeting, the board of directors can decide on the following matters.

The below resolutions shall be adopted by a majority of all the directors:

- adopting resolutions on the issuance of corporate bonds;
- deciding on the company's purchasing its own shares to use shares for employee stock ownership plan or equity incentives;
- deciding on the company's purchasing its own shares to use shares for converting convertible corporate bonds issued by the company; and
- deciding on the company's purchasing its own shares because it is necessary for a listed company to protect the corporate value and the rights and interests of shareholders.

The following resolutions shall be adopted by more than two-thirds of all the directors:

- deciding on the issuance of new shares by not exceeding 50% of the issued shares within three years; but if non-monetary property is contributed as capital at an assessed value, such issuance shall be subject to the resolution of the shareholders' meeting; and
- deciding on the company's providing financial assistance for another person to acquire shares of the company or its parent company; however, the cumulative total of financial assistance shall not exceed 10% of the issued capital stock.

If the board of directors goes beyond the function stipulated in the law or the articles of association, and acts without any proper approvals by the shareholders' meeting, it will constitute a violation with potential damage to the interests of the company in judicial practice.

Decisions of the Shareholder Meeting

In general, the new revision to Company Law narrows the scope of functions of the shareholders' meeting, and creates more rooms for the board of directors, which was appraised by

many commentators as a sign of encouraging professionalism in corporate governance.

The shareholder meeting is responsible for making decisions on fundamental issues, including but not limited to:

- electing and replacing directors and supervisors, and determining their remuneration;
- reviewing and approving plans for the company's dividend distribution and loss recovery;
- amending the articles of association of the company;
- making resolutions on any increase or decrease of the company's registered capital; and
- making resolutions on merger, division, dissolution or liquidation of the company, or change of the company form.

Protection of Bona Fide Counterparts

For the protection of the interests of bona fide counterparts and transaction stability, the Company Law stipulates the following special measures.

- For legal representatives, any restriction on their functions imposed by the company's by-laws or shareholders' meeting cannot be used as an excuse to deny the validity of the company acting against the bona fide counterpart.
- For directors, any restriction on functions of the board of directors in the articles of association cannot be used as an excuse to deny the validity of the company acting against the bona fide counterpart.
- If a people's court declares invalid, revokes, or confirms the untenability of a resolution of a shareholders' meeting or board of directors, a civil legal relation established between the

company and a bona fide counterpart based on the resolution shall not be affected.

- The company cannot use the company registration matter without formal registrations or modifications as an excuse against the bona fide counterpart.

The above provisions mean that, if the bona fide counterpart has justifiable reasons to believe that the company is properly empowered and acts based on such belief, the court shall assume that the actions between the company and the bona fide counterpart are valid.

Protection of Stakeholders' Interests

For the protection of stakeholders' interests, the Company Law stipulates special procedural requirements as a precondition for the following activities of the company, which essentially reflects the multiple layers of competition among the interests of shareholders and external creditors, and those of majority shareholders and minority ones:

- if a company invests in other enterprises or provides guarantees for other external parties, the decision shall be made by the shareholders' meeting or board meeting, per the articles of association of the company; and
- if a company provides a guarantee for its shareholders or actual control persons, the decision shall be made by the shareholders' meeting; the aforesaid shareholders or the shareholders under the control of the aforesaid actual control persons shall not vote on the aforesaid matters; the decision shall be passed by more than half of the voting rights held by the other shareholders present at the meeting.

The Validity of Guarantees by the Company When Legal Representatives Violate Internal Procedures

Article 7 of the Interpretation of the Supreme People's Court of the Application of the Relevant Guarantee System of the Civil Code of the People's Republic of China stipulates that if the legal representative violates the legal procedure of the company providing the external guarantee and exceeds their empowerment to conclude a guarantee contract with the counterpart on behalf of the company, the validity of the guarantee contract shall be determined in accordance with the following criteria:

- if the counterpart is in good faith, the guarantee contract shall be effective for the company; externally, the company shall bear guarantee liability; internally, the company may claim indemnification against the legal representative at fault; and
- if the counterpart is not in good faith, the guarantee contract is not effective for the company.

The counterpart has the obligation to reasonably examine the validity of the company's resolutions. If the counterpart has evidence of its reasonable examination, the people's court shall determine that it acts in good faith, unless the company has evidence showing that the opposite party knows or should know that the resolution is forged or altered.

The criterion for judging the good faith of the counterpart, for a case involving a publicly traded company, is whether the counterpart enters into the guarantee contract based on the information publicly disclosed by the listed company.

3.3 Decision-Making Processes

Normally, meetings of the board of directors shall be convened and presided over by the chair of the board. When the board of directors votes on a resolution, each director shall have one vote.

Procedural Requirements for Board Meetings

For a limited liability company, the discussion methods and voting procedures of the board of directors shall be specified by the articles of association or by-laws, unless it is otherwise provided for by the Company Law.

In joint stock companies, the convening of board meeting shall follow special procedural requirements.

- The board of directors shall convene at least two meetings a year, which must be notified to all directors and supervisors ten days in advance.
- Shareholders representing more than a tenth of voting rights, or more than a third of the board of directors or the board of supervisors, may propose to convene an interim meeting of the board of directors.

For limited liabilities companies and joint stock companies, their board meeting shall follow some procedural requirements.

- No meeting of the board of directors can be held unless more than half of the directors are present.
- When the board of directors makes a resolution, it shall be adopted by more than half of all the directors.

Related-Party Transactions

For the management of related-party transactions, it is clarified that affiliated directors shall recuse themselves from voting; if the number

of non-affiliated directors present at the board meeting is less than three, the related-party transaction shall be submitted to the shareholders' meeting for review and approval.

Voting Deadlock Solution

In practice, if there is a deadlock situation in decision-making, solutions should be clearly stipulated in the articles of association or internal corporate governance rules. For example, the chair of the board can have an additional second voting right, or some key directors can have a veto right.

With respect to the shareholder meeting, please see **5.3 Shareholder Meetings** regarding decision-making processes.

4. Directors and Officers

4.1 Board Structure

The board of directors in a limited liability company shall have at least three members, while there is no upper or lower limit for the number of board members of a joint stock limited company.

- Small companies, a company with a smaller scale or with fewer shareholders may only have one single director, but without the board of directors.
- For medium-to-large companies, if the board of directors has three or more members, it may include an employees' representative. The board of a limited liability company which has 300 or more employees and does not establish the board of supervisors shall include an employees' representative.

Audit Committee or Board of Supervisors

A company may set up an audit committee in the board of directors to exercise the supervisory

functions and powers to replace the board of supervisors or supervisor. The audit committee of a joint stock company shall have at least three members.

4.2 Roles of Board Members

The board of directors shall be presided over by a chair, and may have one or more vice-chairs. The chair shall be responsible for presiding over shareholder meetings, convening and presiding over meetings of the board of directors, and inspecting the implementation of resolutions of the board. A vice-chair assists the chair in their work. If the chair cannot or does not carry out their duties, such duties shall be carried out by the vice-chair; if the vice-chair cannot or does not carry out its duties, the duties shall be carried out by a director jointly elected by more than half of the directors.

A publicly traded company shall have independent directors and board secretaries. Independent directors shall be responsible for supervising the directors and officers, and shall report their work to the shareholder meeting annually. The board secretary shall be responsible for the preparation of shareholder meetings and meetings of the board of directors, custody of documents, management of shareholders' materials, disclosure of information, investor relations and other matters.

4.3 Board Composition Requirements/Recommendations

Qualifications of Directors

Persons may not serve as a director of a company in any of the following circumstances:

- they are without civil capacity or have limited civil capacity;
- they have been sentenced to criminal penalties for corruption, bribery, embezzlement or

misappropriation of property or for sabotaging the socialist market economy order, and less than five years has elapsed since the expiration of the period of execution, and less than two years has elapsed since the expiration of the probation period of suspended sentence;

- they have been deprived of their political rights for committing a crime, and less than five years has elapsed since the expiration of the period of execution;
- they have served as a director or manager of an enterprise that has been declared bankrupt and they bear personal responsibility, and less than three years has elapsed since the date of completion of the bankruptcy liquidation;
- they have served as the legal representative of an enterprise whose business licence has been revoked or has been ordered to close its business operations due to a violation of law and bear personal responsibility, and less than three years has elapsed since the date of the revocation of business licence or the date of the order of closing down; and
- they have been listed by the people's court as the persons subject to the enforcement for breach of trust obligations because they have a large amount of debt, which is due but has not been repaid.

Special Requirements for Chairman and Staff in Certain Industries

There are special senior position segregation requirements in specific industries. For an example, the chairman of a bank or an insurance company shall not concurrently serve as the CEO or the general manager for the institution. And members of commercial banks and state-owned companies may not take part-time jobs in other economic organisations.

4.4 Appointment and Removal of Directors/Officers

The directors who are not representatives of the employees shall be appointed and removed by the shareholder meeting. The employees' representatives shall be democratically elected by the employees through the employees' congress, through the employees' meeting or in other ways. The method of appointing the chair and vice-chair of the board of directors in a limited liability company shall be stipulated in the articles of association of the company.

In practice, the chair and vice-chair can be elected or recommended by the shareholder meeting or the board of directors. The chair and vice-chair of the board of directors in a joint stock limited company are elected by more than half of all the directors on the board of directors.

The manager shall be appointed and removed by the board of directors. The appointment and removal of the deputy manager and chief financial officer shall be recommended by the manager and decided by the board of directors.

Legal Representative

For the legal representative, the new revision to Company Law has special provisions.

- The legal representative of a company shall be a director or general manager who carries out business on behalf of the company.
- If a director or manager who serves as the legal representative resigns, they shall be deemed to have resigned from the legal representative position at the same time. If the legal representative resigns, the company shall appoint a new legal representative within 30 days from the date of resignation.
- The articles of association of a limited liability company shall specify the methods of

appointing and replacing the company's legal representative.

The new revision to Company Law expands the scope of candidacy of legal representatives beyond chairpersons or the CEO, and resolves a potential difficult situation that the legal representative may not be available for performing duty if no successor to the chair or CEO is available. The new revision also encourages the diversity of members of board of directors. If there is no substantial interest relationship between the registered legal representative and the company, and the legal representative is not involved in any actual business operation, the legal representative can file a deregistration lawsuit.

4.5 Rules/Requirements Concerning Independence of Directors

As a general rule of fiduciary duty, directors must act with good faith and independently for the best interests of the company. Regarding the rules or requirements concerning independence of directors, the current regulations about independent requirements are mainly for the independent directors.

Independent Director Requirements

Independent directors of publicly traded companies are required to meet the general requirements for directors as stipulated in the Company Law, as well as the specific qualifications for independent directors under regulatory supervision rules applicable for publicly traded companies.

- Persons who work or provide services in the publicly traded company, its controlling shareholders, its actual control persons, or their respective subsidiaries and their related persons, or persons who have significant

business dealings with the above-mentioned enterprises, or persons who work in companies having significant business dealings with the above-mentioned enterprises, their controlling shareholders or their actual control persons shall not serve as independent directors.

- Persons holding the position of independent director shall have more than five years of working experience in law, economics or another field, and having no records of major breaching of promises or other illegal records.

In addition, there are limitations for some people with a conflict of interest to be an independent director. For example, within three years after resigning or retiring (leaving), leading officials in middle management of the company shall not be appointed as independent directors or independent supervisors of publicly traded companies to avoid potential conflicts.

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors and officers of a company are the fiduciary duties – ie, the duty of loyalty and the duty of diligence. The new revision to Company Law clarifies, for the first time, the connotations of the duty of loyalty and the duty of diligence.

The Duty of Loyalty

The duty of loyalty requires directors and officers to take measures to avoid conflicts between their own interests and the company's interests, and not to take advantage of their powers to pursue improper interests, with the following important restrictions:

- directors and officers and their close relatives, and enterprises directly or indirectly controlled by them, and persons who have other affiliated relationships with them, shall not

enter into contracts or engage in transactions with the company they are serving without the consent of shareholder or board meetings;

- without the consent of shareholder or board meetings, directors and officers shall not seek business opportunities that would have belonged to the company for themselves or others by taking advantage of their position; and
- without the consent of shareholder or board meetings, directors and officers shall not engage in business that is similar to the company's, for themselves or others.

Any income arising from the breach of duties of loyalty shall belong to the company.

The Principle of Business Judgement

The new revision to Company Law adds a specific interpretation of the duty of diligence, which indicates that the directors and officers shall act as reasonable business persons do. The principle of business judgement also leaves room for Chinese courts to determine what will be the reasonable level of business judgement for Chinese company directors.

4.7 Responsibility/Accountability of Directors

Directors are required to take into account the overall interests of the company and the interests of all shareholders when discharging their duties. In publicly traded companies, the directors are required to pay special attention to the interests of the minority shareholders, as well as other interested parties, such as creditors, employees, clients, suppliers and communities.

Director Accountability Exemption

In a joint stock company, the directors shall be responsible for the board resolutions. If a resolution violates laws, administrative regulations, the

articles of association or the resolution of the shareholders' meeting, and its execution causes serious losses to the company, the directors participating in the resolution shall be liable for loss compensation to the company.

However, if it is proved, as normally recorded in the board meeting minutes, that a director has expressed their objection at the time of voting, that director may be exempted from liability.

4.8 Consequences and Enforcement of Breach of Directors' Duties

If directors or officers breach their duties, they may face the following consequences:

- internal disciplinary action;
- shareholder lawsuit;
- administrative punishment; and
- civil liability and criminal punishment.

Shareholder Derivative Lawsuits Against Directors or Officers

If directors or officers breach their duties and thereby cause losses to the company or its wholly-owned subsidiaries, the shareholder(s) of the limited liability company, or shareholders individually or collectively holding 1% or more of the total shares of a joint stock company for 180 consecutive days or more, may request the board of directors or board of supervisors in writing to file a lawsuit against the responsible directors or officers.

If the board of supervisors or board of directors does not file a lawsuit or in an emergency, shareholders satisfying the aforesaid conditions have the right to file a lawsuit in their own name representatively, in the interests of the company.

If a shareholder brings a lawsuit against a director, an officer or other persons in accordance

with the above procedures, the company shall be listed as a third party to participate in the lawsuit.

Circumstances of Director or Officer Breaching Fiduciary Duty

There are legal bases for shareholder derivative lawsuits against directors or officers for breaching corporate governance requirements:

- directors or officers shall be liable for compensation if they injure the interests of the company by taking advantage of their connection relationship;
- responsible directors and officers shall be liable for compensation if they fail to promptly perform the obligation of checking and supervising the shareholders' fulfilment of capital contribution obligation;
- responsible directors and officers shall be jointly and severally liable for compensation with the shareholder if the shareholder withdraws their capital contribution and causes losses to the company;
- responsible directors and officers shall be liable for compensation for losses caused to the company if the company distributes profits to shareholders in violation of the law;
- responsible directors and officers shall be liable for compensation if the company provides financial assistance for another person to illegally acquire shares of the company or its parent company and causes losses to the company;
- responsible directors and officers shall be liable for compensation for losses caused to the company if registered capital is reduced in violation of the law; and
- the director with obligations of liquidation of the company shall be liable for compensation if they fail to perform their liquidation

obligations in time and cause losses to the company.

Shareholder Direct Lawsuit Against Directors or Officers

If directors or officers violate any law, administrative regulations or the company's articles of association, thereby harming the interests of a shareholder, the shareholder may directly file a lawsuit, in their own interests.

Company Lawsuits Against Directors or Officers

A company can directly sue its directors or officers for their failure to fulfill their duty of loyalty and diligence.

For example, Article 13 of Provisions of the Supreme People's Court on Several Issues Concerning the Application of the Company Law of the People's Republic of China (III) stipulates that if a shareholder fails to fulfil the capital injection obligation at the time of the company's capital increase, the company can request the directors or officers who fail to monitor or manage the process to pay the capital; after the directors or officers repay the capital, they may claim indemnification against the defendant shareholders.

With respect to the shareholder direct lawsuits against company itself, please see **5.4 Shareholder Claims**.

Class Action Lawsuit in Securities Litigation

Directors and officers of publicly traded companies, along with the company and other responsible parties, may also be held accountable for misbehaviour including false statements, breach of promises, insider trading and market manipulation, and shall be responsible to compensate the investors who have suffered losses as a result of such conduct, according to the

following special procedures of shareholder representative lawsuits under the Securities Law of China. The lawsuits are similar to class action lawsuits in western developed markets but with special procedures.

- If an investor protection institution holds shares of the company, the institution may file a lawsuit in its own name in the interests of the company with no limitations on the shareholding ratio and holding period.
- If the parties on one side of the actions are numerous with the same type of claims, they may legally recommend and select representatives to participate in the actions; the people's court may issue an announcement to notify the investors to register during a certain period.
- An investor protection institution, authorised by 50 or more investors, may participate in actions as a representative, except for investors who have expressly indicated their reluctance to participate in the actions.

Furthermore, the China Supreme People's Court issued a judicial interpretation in 2022 stipulating that such civil litigation does not need to wait until an administrative authority or criminal court makes a formal finding on the wrongfulness of the alleged misconduct.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

There are other bases for claims or enforcement against directors or officers according to new revisions of Company Law, which already cause attention from the public.

Claims Against Legal Representatives

If the legal representative causes damage to others due to the performance of their duties:

- externally, the company shall bear civil liability; and
- internally, the company may claim indemnification against the legal representative at fault.

That means, for the protection of the legal representative in the performance of their duty, normally the plaintiff is required to first bring a case against the company itself instead of the legal representative.

Liability to Third Parties for Directors or Officers Performing Duties

If a director or an officer acts in their official capacity and causes damage to other third parties, the company shall be liable for compensation.

Directors and officers who have malign intention or act with gross negligence shall also be liable for compensation.

Either the company or its directors or officers can be listed as defendant in the lawsuit.

In reality, it is expected that both the company and its directors and officers will be listed as co-defendants at the same time as a result of litigation strategy. It is more clear, however, that the company will normally bear the responsibility first. It will be the company's decision on whether to claim indemnification against directors, officers or the legal representative.

Claims Against Controlling Shareholders and Actual Control Persons (Shadow Shareholders and Shadow Directors)

In addition, the new revision to the Company Law adds the following liabilities of controlling shareholders and actual control persons. To some extent, this revision tries to solve some serious governance problems caused by Shad-

ow Shareholders or Shadow Directors who are manipulated by controlling shareholders or actual control persons in practice.

- The other shareholders shall have the right to request the company to acquire a controlling shareholder's equities, who abuses shareholder rights with prejudice to the interest of the company or other shareholders, at a reasonable price.
- The controlling shareholders or actual control persons of the company who do not serve as its directors but attend to the company's affairs shall also undertake duties of loyalty and diligence.
- The controlling shareholders or actual control persons instruct a director or officer to engage in any act against the interests of the company or shareholders, the controlling shareholders or actual control persons shall be jointly and severally liable.
- From the perspective of actual shareholders having significant influence over the company's operation and management, it is worthwhile to further explore the issue of recognising them as substantive directors, or recognising them as having the same liquidation obligations as directors.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

According to the Company Law, remuneration, fees or benefits payable to directors are decided by the shareholder meeting. Payments to the manager are decided by the board of directors, and payments to the deputy manager and chief financial officer are decided by the board of directors upon proposals by the manager.

In a publicly traded company, when the board of directors or the remuneration and assessment

committee is evaluating the performance of a director or is discussing their compensation, the director shall not participate in such evaluation or discussion. The remuneration distribution plan for officers shall be approved by the board of directors, explained at shareholder meetings and fully disclosed.

Incentive Payment and Deferred Payment

Financial institutions such as banking and insurance institutions have deferred remuneration requirements for directors, officers and key positions. In general companies, this kind of mechanism can also be stipulated through the articles of association to limit such incentive payment.

4.11 Disclosure of Payments to Directors/Officers

According to the Company Law, a joint stock limited company shall regularly disclose to its shareholders the remuneration, fees or benefits payable to directors and officers. A publicly traded company shall disclose the appointments, changes of shareholding and annual remuneration of its directors and officers in its annual report.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Shareholders mainly have the following rights with regard to the company.

- The right to income:
 - (a) dividend claims;
 - (b) residual claims;
 - (c) pre-emptive rights for new shares;
 - (d) dissenting shareholders' right to request repurchase of shares; and
 - (e) pre-emptive rights for shares sold by

other shareholders in limited liability companies.

- Voting rights and related rights:
 - (a) voting rights;
 - (b) rights to attend shareholder meetings;
 - (c) rights to propose to convene interim shareholder meetings and meetings of the board of directors; and
 - (d) rights of proposal.
- The right to know and other rights.

Shareholders' Obligation

The shareholders' principal obligation to the company is to invest capital in accordance with their committed payment schedule provided in the articles of association of the company.

Shareholders' Civil Liabilities

Shareholders who fail to fulfil their investment obligations may bear civil liabilities, and directors, officers and promoters may also be jointly liable.

- After the formation of a company, no shareholder can withdraw the capital investment. Directors and officers have the responsibilities of managing the capital. If losses are caused to the company by late payment or capital withdrawal, the directors and officers shall be held jointly and severally liable.
- If a shareholder fails to complete its capital contribution on schedule, the company shall issue a written demand to the shareholder to demand payment of capital contribution. If the shareholder fails to perform the obligation after expiration of the grace period, the shareholder shall forfeit the rights to the unpaid equity or shares on the date of issuance of the notice.
- Acceleration of contribution – if the company is unable to pay off its due debts, the company or creditors of the due debts shall have

the right to require the shareholders to pay the capital contributions before expiration of the period of payment of capital contribution. For *“the right to require the shareholders to pay the capital contributions”* in the new Company Law, the shareholders could still be ordered to pay the creditors directly in the current judicial practice.

- The other promoters shall be jointly and severally liable with the promoter who fails to pay the subscription in accordance with the shares they have subscribed for, or when the actual value of the non-monetary property as capital contribution is significantly lower than the the shares subscribed for.
- In the case of an equity transfer where the capital contribution is not due after the implementation of the new Company Law, if the transferee fails to fully pay the capital contribution on time, the original shareholders shall bear supplementary liability to the creditors for the portion of the insufficient capital contribution.

Shareholders' Criminal Responsibilities in Capital Contribution

According to the Criminal Law, shareholders who fail to fulfil their investment obligations may bear criminal responsibilities for making a false capital contribution or withdrawing the contributed capital. According to a legislative interpretation, the rule only applies to companies that legally implement the paid-in system of registered capital. Shareholders of joint stock companies shall pay more attention to this criminal liability of capital contribution.

The Boundaries of Shareholders' Rights: Piercing the Corporate Veil

The shareholders shall not abuse the independent legal person status of the company and

limited liabilities of shareholders to damage the interests of the company's creditors.

- Shareholders, instead of the company itself, may be directly held jointly liable if evidence shows shareholder and company personality confusion, excessive dominance or control by shareholders in company management, or that the capital is significantly insufficient.
- If shareholders use two or more companies under their control to evade debts, each company shall be jointly and severally liable for the debts of any company.
- The company which has only one shareholder which cannot prove that the property of the company is independent of their own property, shall be jointly and severally liable for the debts of the company.

In the case of company personality confusion, the denial of personality may result in the parent and subsidiary being jointly and severally liable for each other's debts because the boundary between the shareholders' property and the company's property is unclear. This approach of *“reversely piercing the corporate veil”* should be limited to the specific situation of legal personality confusion.

5.2 Role of Shareholders in Company Management

Ownership of companies is somewhat separated from management rights. The managers are responsible for the operation and management of the company while, as owners of the company, shareholders do not normally participate directly in the daily operation and management of the company. Their management in a company is indirect, which means they exercise their rights in a collective manner by participating in shareholder meetings and voting on proposals in accordance with the procedures provided by

laws and the articles of association of the company. The shareholders may make decisions on fundamental issues and elect the main members of the board of directors by exercising their voting rights and thereby control the company.

As a common business practice, share repurchase plays an important role in adjusting the shareholding structure of enterprises and protecting investors' rights.

If both parties agree on the period during which the investor requests the other party to repurchase, the period should be recognised in accordance with the principle of good faith even though the reasonable expectation is no more than six months since the triggering event for repurchase happens.

5.3 Shareholder Meetings

Generally, shareholder meetings are convened by the board of directors and presided over by the chair of the board.

- If the board of directors is unable or fails to perform its duty of convening a shareholders' meeting, the board of supervisors shall convene and preside over the meeting.
- If the board of supervisors does not convene and preside over the meeting, the shareholders representing more than one-tenth of the voting rights in a limited liability company, or shareholders who individually or collectively hold more than 10% of the company's shares for more than 90 consecutive days in a joint stock company may convene and preside over the meeting on their own.

However, a decision may be made without convening a shareholder meeting if shareholders unanimously agree in writing (all shareholders sign and seal on the resolution documents).

Voting Rights Required for Adopting a Resolution by Shareholder Meeting

If there is no special provision in the articles of association of the company, all the shareholders shall be notified 15 days before a shareholder meeting is held, and the shareholders shall exercise their voting rights at the meeting in proportion to their capital contribution.

Normally when the shareholders' meeting makes a resolution, it shall be adopted by shareholders representing more than half of the voting rights.

Specially, some resolutions shall be approved by shareholders representing more than two thirds of voting rights:

- deciding on the amendment of the articles of association, increases/decreases of registered capital, mergers, divisions, dissolution or changes of the company form;
- a publicly traded company purchasing or selling significant assets, or guaranteeing an amount exceeding 30% of the company's total assets within one year; and
- issuing classified shares different from the rights of ordinary shares.

There are special voting approaches such as cumulative voting, which can also be used in the shareholders' meeting according to Chinese Company Law.

5.4 Shareholder Claims

Shareholders, on behalf of the company or its wholly owned subsidiaries, can file derivative lawsuits against a company's directors, officers or others outside the company for the company's losses. The specific procedure can be seen in **4.8 Consequences and Enforcement of Breach of Directors' Duties** regarding shareholder lawsuits against directors or officers.

Shareholder Direct Lawsuits

Shareholders can file shareholder direct lawsuits against the company itself based on civil liability for torts.

- If the company refuses to provide shareholders access to inspecting or copying legal documents or materials of the company without justifiable reasons, the shareholders may file a lawsuit to the people's court; specifically, the legal documents or materials include: the articles of association, the register of shareholders, the minutes of shareholders' meetings, the resolutions of the board of directors, the resolutions of the board of supervisors, financial accounting reports, accounting books, accounting records, and related materials of wholly-owned subsidiaries; and according to the new revision of the Company Law, shareholders are allowed to entrust intermediaries to act on their behalf.
- In cases where a shareholder requests confirmation that a resolution of the shareholders' meeting or board meeting is not established, invalid or revoked, the company shall be listed as the defendant.
- In a case where a shareholder requests a company to distribute profits, the company shall be listed as the defendant; if the shareholder fails to submit a resolution of the shareholders' meeting specifying a specific distribution plan, the people's court shall reject their claim, except when the company does not distribute profits in violation of the law and causes losses to other shareholders.

5.5 Disclosure by Shareholders in Publicly Traded Companies

In some situations, a shareholder or actual control person of a publicly traded company shall inform the board of directors and co-operate

with the company in performing information disclosure obligations:

- of a relatively significant change in the control of the company, or the shareholding of shareholders who hold more than 5% of the company's shares, or the actual control person;
- of a relatively significant change in the situation of engagement in business identical or similar to the company that is taken by the company's actual control person and other enterprises controlled by the actual control person;
- if the controlling shareholder was prohibited from transferring their shares by a court ruling or judgment;
- if more than 5% of the company's shares held by any shareholder are pledged, frozen, judicially auctioned, kept in custody or established in trust, or their voting rights are restricted, or there is a risk of being forced to transfer ownership; and
- of a plan to significantly restructure assets or business of the publicly traded company.

The CSRC also requires that, where any shareholder of the company applying for an IPO has a shareholding structure consisting of two or more layers and is a company or a limited partnership with no actual business activities, the ultimate beneficial owner of such shareholder should be disclosed, in the case that the buy-in price of such shareholder is apparently abnormal.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Publicly traded companies are subject to periodic financial reporting (annual, midterm and

quarterly reports) and interim financial reporting requirements.

Directors/Officers Responsibilities in Financial Reporting

The contents of the periodic report shall be examined and approved by the board of directors. The directors and officers of the company shall sign written confirmation opinions on the periodic report, and the board of supervisors shall submit written review opinions on the periodic report.

If the directors or supervisors are unable to guarantee the authenticity, accuracy and completeness of the periodic report or have objections, they shall vote against or abstain from voting. Directors and officers are not absolutely relieved of their responsibility if they cannot closely follow the principle of prudence during the report preparation and disclosure.

Gatekeeper Responsibilities

China securities regulations also strengthen the gatekeeper responsibility of intermediary institutions, which generally include securities companies and their personnel as sponsors and/or underwriters, securities service agencies, law firms, accounting firms, and asset evaluation agencies.

In practice, shareholder class action lawsuits can be filed against the company, directors, officers and intermediary institutions for their breach of duties in cases of false statements, breach of promises, insider trading and manipulation of the market.

6.2 Disclosure of Corporate Governance Arrangements

There are some requirements for publicly traded companies to disclose their corporate govern-

ance arrangements in the midterm report and annual report.

In the midterm report, a publicly traded company shall disclose its corporate governance arrangements, including:

- the annual shareholder meeting and interim shareholder meetings held during the reporting period;
- the removal of directors, supervisors and officers, as well as the reasons for doing so, during the reporting period;
- whether the dividends distribution plan and the plan for conversion of capital reserve fund to share capital comply with the articles of association and provisions for review procedure, and have adequately protected the legitimate interests of the minority investors, and whether the independent directors have issued opinions; and
- the implementation of an equity incentive plan, employees' stock holding plan or other incentive measures for employees during the reporting period.

In addition to the arrangements mentioned above, a publicly traded company shall also disclose the following in its annual report:

- the measures that the controlling shareholder and actual control persons take to guarantee the independence of the company;
- the situation of engagement in business that is identical or similar to the company that is taken by the controlling shareholder, actual control persons and other enterprises controlled by them;
- the implementation of and changes to the arrangements on difference in voting rights during the reporting period;

- basic information on and annual remuneration of directors, supervisors and officers;
- meetings of the board of directors held during the reporting period and the performance of each director;
- the membership of the special committees under the board of directors, and meetings of special committees held during the reporting period;
- opinions of the board of supervisors on supervision matters during the reporting period;
- employees of the company's parent company and its main subsidiaries;
- the construction and implementation of the internal control system during the reporting period; and
- management of its subsidiaries during the reporting period.

6.3 Companies Registry Filings

The new revision to the Company Law takes dual approaches to capital contribution for limited liability companies and joint stock companies, which means:

- for limited liability companies, the subscribed capital shall be paid fully by its shareholders within five years from the date of the company's establishment; and
- for joint stock companies, the paid-in capital system applies (promoters shall pay in full for their subscribed shares before the date of the company's establishment).

Joint stock companies established by public offering are required to submit a capital verification certificate from a capital verification institution when applying for company registration.

It should be noted that a company shall provide official registry with necessary information for

company registration and licence. The company shall also formally file registration or modification documents for its registration matters before it can leverage them against any bona fide counterparts.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

A company shall prepare a financial statement at the end of each fiscal year, which shall be audited by an accounting firm in accordance with relevant law. According to the articles of association of the company, the decision to hire or dismiss the accounting firm that undertakes the company's auditing business shall be taken by the shareholder meeting or the board of directors. When the shareholder meeting or the board of directors votes on the dismissal of the accounting firm, the accounting firm shall be allowed to state its opinions.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls Small Companies

The key requirements for directors in connection with internal controls in small companies are based on Internal Control Norms for Small Companies issued by the Minister of Finance in 2017.

- Compared with the principle of comprehensiveness, importance and balance of internal control of large and medium-sized companies, the special principles of internal control for small companies are risk oriented and focus on substantial risks.
- Compared with the complex internal control measures of large and medium-sized companies, key position separation, internal authorisation and approval process, accounting and

financial control, documentation and invoice control are essential for small companies.

Large and Medium-Sized Companies

The board of directors shall be responsible for the establishment and implementation of internal controls. The board of supervisors shall supervise the establishment and implementation of internal controls by the board of directors. Managers shall be responsible for organising and leading the day-to-day operation of the company's internal controls. A company shall establish a special department or designate an internal department to be specifically responsible for organising and co-ordinating the establishment and implementation of internal controls and daily work.

Publicly Traded Companies

Special requirements for directors in connection with the risk management and internal controls in publicly traded companies include the following.

- In respect of corporate governance structure, a publicly traded company shall have independent directors and board secretaries, and its board of directors shall establish an audit committee; it may also establish special committees on strategy, nomination, remuneration and assessment.
- In respect of voting rights, the board of directors, an independent director or shareholders holding 1% or more of the voting shares of

a listed company or an investor protection institution may, as a proxy solicitor, publicly request the shareholders of the listed company to authorise it to attend a shareholders' meeting and exercise the shareholders' right. The company and the convenor of the shareholders' meeting shall not set a minimum shareholding limit on the voting rights of shareholders. The solicitor shall disclose solicitation documents, and the listed company shall provide co-operation.

- In respect of information disclosure, a publicly traded company shall disclose the assessment report on internal control approved by the board of directors, and the audit report on internal control over financial reporting issued by the accounting firm at the same time as the annual report. The specific contents of periodic and interim reports can be seen in **6.1 Financial Reporting** and **6.2 Disclosure of Corporate Governance Arrangements**.
- For independent directors, the specific discussion can be seen in **4.5 Rules/Requirements Concerning Independence of Directors**.

Overall, with the new Company Law, Chinese companies are given more autonomy in their corporate governance, which leaves more room for them to design their articles of association and to determine the best rules for themselves. It also creates more battlefields for participants in Chinese companies' corporate governance.

COLOMBIA

Law and Practice

Contributed by:

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Baker McKenzie S.A.S.



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Baker McKenzie S.A.S. has been present in Colombia for 80 years and is a leading figure in the legal landscape of South America. Its office in Bogotá works on cross-border transactions with the Baker McKenzie network in the region and across the globe, primarily with the London office as well as the New York, Chicago, Houston and West Coast offices in the US, seamlessly supplying its clients with relevant and effective advice. It assists national and multina-

tional companies with the legal needs of their businesses in the country and abroad. Having acted in some of the country's largest transactions and projects, it is recognised as one of the top legal advisers in the country. It has global capabilities and an instinctively global mindset which gives it the ability to embrace complexity across boundaries with pragmatism, ease and sophistication. Being global is really a part of its DNA and has been its defining focus.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The most common structures to conduct business in Colombia are: (i) the simplified stock company (S.A.S.); (ii) the corporation (*sociedad anónima*); (iii) the limited liability company (Ltda); and (iv) the branch of a foreign company.

A summary of the main characteristics of the most commonly used vehicles is set out below.

Simplified Stock Company or “S.A.S.”

A S.A.S. requires at least one shareholder and is incorporated by private document and registered at the local trade register. This is unless assets are being contributed at the time of incorporation. In this case a public deed is required for transfer (eg, real estate). The S.A.S. is a modern and flexible structure, providing the parties with greater freedom to agree the rights of, and restrictions on, shareholders. It is used for small single owner companies, multinational subsidiaries, family companies and joint ventures, among others.

The corporate purpose may be broadly defined and the term of the corporation can be indefinite. Liability is limited to the capital contribution in the absence of fraud or abuse.

Capital is represented in shares. The transfer of shares is carried out by endorsing the share certificates or issuing a letter of instructions and registering the new shareholder in the company's stock ledger. Share issues and transfers may be subject to a right of first refusal in favour of the company and the shareholders, if expressly set out in the by-laws. A board of directors is optional but a statutory auditor must be appointed when certain thresholds are met.

Corporation or “S.A.”

An S.A. corporation requires a minimum of five shareholders. None of the shareholders may hold 95% or more of the outstanding capital of the company. It is incorporated by public deed granted before a Colombian Public Notary and registered at the local trade register.

Corporations must define the corporate purpose and a fixed term in the by-laws. A board of directors and statutory auditor is compulsory. This is the traditional type of stock corporation and is used for listed companies and banks, among others.

Capital is represented in shares. Liability is limited to the capital contribution in the absence of fraud or abuse. The transfer of a corporation's shares is carried out by endorsing the share certificates or issuing a letter of instructions and registering the new shareholder in the company's stock ledger. The transfer may be subject to a right of first refusal in favour of the company and the shareholders, if agreed in the by-laws. There is less freedom to agree different rules on the company structure, meetings, dividend distribution, reserves etc as these are regulated under the Colombian Commercial Code.

Limited Liability Company (Ltda)

This type of company must have at least two and no more than 25 partners. It is incorporated by public deed granted before a Colombian Public Notary and has to be registered with the local trade register.

Limited liability companies must define the corporate purpose and a fixed term in the by-laws. This type of company has fallen into disuse since the simplified stock company became available in 2008. However, it is still used in specific industries and sectors where this structure is required.

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Capital is represented in quotas, which can only be transferred on exercise of a mandatory first right of refusal, amendment of the by-laws and registration in the public register. Liability for tax and employment matters can extend to those holding quotas in these types of companies. There is less freedom to agree different rules on the company meetings, dividend distribution, reserves etc as these are regulated under the Colombian Commercial Code. A board of directors is optional but a statutory auditor must be appointed when certain thresholds are met.

Branch of a Foreign Company

Branches are part of the same legal entity abroad (or home office) that sets up the branch so there is no limitation of liability. The board resolutions of the home office are incorporated into a public deed which is granted by a Colombian Public Notary and registered at the local trade register.

Corporate purpose will be narrowly defined and be within the home office's corporate purpose. The corporate purpose must be defined. Branches are frequently used in the oil and gas sector and for public procurement.

1.2 Sources of Corporate Governance Requirements

Colombian legislation does not establish mandatory governance codes or equivalent for privately owned companies or groups of companies.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with publicly traded shares must comply with the following corporate governance requirements.

Boards of directors must have between five and ten members. At least 25% of the members

must be independent, which means that they cannot be:

- employees or officers of the company or of any of its affiliates, subsidiaries or controlling companies, including those individuals who have had this capacity throughout the year immediately preceding the appointment, except in the case of the re-election of an independent person;
- shareholders who directly or by means of an agreement direct, guide or control the majority of the voting rights of the entity or who determine the majority composition of the administrative, management or control bodies of the entity;
- a partner or employee of associations or companies that provide advisory or consulting services to the issuer or to the companies that belong to the same economic group of which it is part, when the income for the concept represents 20% or more of their operational income;
- an employee or director of a foundation, association or society that receives significant donations from the issuer (significant donations are considered to be those that represent more than 20% of the total donations received by the respective institution);
- an administrator of an entity in whose board of directors a legal representative of the issuer participates; and
- a person who receives any remuneration other than fees from the company as a member of the board of directors, the audit committee or any other committee created by the board of directors.

When a plurality of shareholders representing at least 5% of the subscribed shares submit proposals to the board of directors of the registered companies, these bodies must consider them

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and respond in writing to those who have made them, clearly stating the reasons for the decisions.

These companies will establish an audit committee, which will be composed of at least three members of the board of directors, including all independent members. The statutory auditor of the company will be present in this committee and will be able to speak but will not be able to vote. The committee will be in charge of supervising compliance with the internal audit programme and will ensure that the preparation, presentation and disclosure of financial information complies with the provisions of the law.

Listed companies must submit an annual and a quarterly report on environmental, social and governance (ESG) matters to the National Registry of Securities and Issuers (RNVE).

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Throughout 2023 and 2024 there were several hot topics in corporate governance that had to be considered. These were aimed at improving sustainability, transparency and responsibility within companies.

ESG

Even though only listed companies must comply with mandatory ESG reporting, the implementation of sustainable policies has become crucial for all types of companies for a number of reasons, including:

- to enhance brand and customer loyalty generating a competitive advantage;
- to attract and retain talent as employees choose to work in a workplace that aligns

with their values and has a supportive environment;

- cost and operational efficiencies: policies that reduce carbon footprint and improve the supply chain can lead to a cost saving, making companies more efficient;
- risk management: reputational and regulatory risk can be controlled by the implementation of policies that address issues that impact stakeholders; and
- attraction of investment: more robust governance and investor protection is becoming a prerequisite for outside investment.

In 2023, the Superintendence of Companies introduced non-mandatory regulations on reporting for unlisted companies that meet certain asset and revenue thresholds and operate in the construction, mining and other sectors. It also issued a new voluntary Sustainability Report for activities in 2024. Additionally, in 2025 it issued regulations creating a new format No 8 to report on sustainability, corporate governance and other legal and administrative matters in companies. These matters were previously reported by filing a business practices report, which has been eliminated. The filing of the sustainability report under the new format is voluntary in 2025 but it is likely to become mandatory in the near future.

Conflicts of Interest

According to Colombian regulations introduced in early 2024, when a legal representative or an administrator, such as a board member, may have a conflict of interest, all relevant information must be disclosed to the shareholders so that they can decide whether to waive the conflict, thereby releasing the legal representative from responsibility, and whether a general authorisation can be granted.

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In December 2024, a draft bill was presented to the Colombian legislature to update corporate regulations. It introduced new rules on administrators' duties and a broader definition for conflicts of interest, which will include events where the administrator has an economic interest in the operation, which could impair their judgment and independence.

The liability regime for administrators could now be extended to shareholders with personal interests if the company suffers damage. Administrators may also face compensatory damages for bad faith in requesting authorisations.

Liability Regime of Administrators

The liability regime of administrators applies to legal representatives, liquidators, members of boards of directors and any individual who exercises these duties in line with the by-laws of the company because they are considered corporate administrators. The business judgment rule was formally recognised in Colombian regulations in Decree No 46 of 2024 (see 4.6 Legal Duties of Directors/Officers).

Other hot topics are:

- compliance (which includes the SAGRILAF and transparency programmes);
- diversity and inclusion policies; and
- digital transformation and how technology can be used to improve efficiency.

2.2 ESG Considerations

It is not currently compulsory for unlisted companies to report on ESG issues. However, the Superintendence of Companies issued External Circular 100-000010 on 21 November 2023 (the "Circular") adding a further Chapter XV on ESG reporting to its Basic Legal Circular.

This Chapter establishes the recommendations to be considered by companies when preparing the sustainability report. The Superintendence of Companies has not yet established dates for when this information has to be filed. However, it issued guidelines in March 2025 for the voluntary filing of a Sustainability Report for the fiscal year 2024. The recommendations are aimed at companies that meet certain thresholds, ie, companies that are subject to the permanent supervision or control of the Superintendence of Corporations and that have reached total income or assets equal to or greater than 40,000 minimum wages, as of December 31 of the immediately preceding year and companies in the mining, manufacturing, construction, tourism and new technologies with revenue of 30,000 minimum wages. Reports must be based on international standards.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The legal representatives of the company (usually called general managers) are responsible for the day-to-day affairs of the business. As legal representatives they are able to legally bind the entity with third parties.

Board of Directors

Board members do not have individual authority to bind the company but instead form a consultative body for planning, setting long-term goals, managing risks and supervising the management. When a company does not have to have a board of directors the functions of the board are assumed by the shareholders' assembly.

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Shareholder' Assembly

The shareholder' assembly is the governing body of the company and is usually responsible for considering annual accounts prepared by the management, appointing directors and legal representatives when the company does not have a board of directors. It is also usually responsible for approving by-law amendments, setting economic guidelines for the business, starting corrective actions against the management and making decisions on the profits.

3.2 Decisions Made by Particular Bodies

General managers must seek to improve a company's performance and profitability and implement the strategy and vision of the company. They will hire employees, sign contracts (subject to any limitations in the by-laws) and prepare financial statements. Additionally, they are responsible for the day-to-day activities.

Boards of directors are usually involved in decisions concerning budgets, strategic decisions, review of annual accounts, share issues, approval of indebtedness, acquisition of relevant assets, appointment of management and authorisations of specific contracts.

Boards of directors are not mandatory for all types of companies in Colombia. When a board is included in the by-laws, rules for the issuance of shares, appointment of management and the issuing of authorisations to managers to enter into contracts restricted by a company's by-laws are decisions usually reserved to this particular body.

The shareholder' assembly adopts all other decisions, including approval of all by-law amendments, annual financial statements, appointment of officers, including the statutory auditor and considerations of conflicts of interest.

3.3 Decision-Making Processes

The shareholder' assembly and the board of directors can make decisions by holding in-person or virtual meetings. Decisions can also be made by written ballots provided that all shareholders or all directors participate. In this case, the legal representative of the company must send the necessary information to allow the directors or shareholders to vote and ensure the timing and other legal provisions are met.

All decisions adopted in a meeting or by written ballot must be reflected in minutes which must be signed by the individuals authorised for this purpose or the individuals provided for in the law.

In principle, decisions of the shareholder' assembly require the affirmative vote of the majority of the shares represented at the meeting. However, the law provides that qualified majorities apply for certain decisions and certain types of entities.

For example, simplified stock companies (S.A.S.) require a unanimous vote to modify provisions in the by-laws that: i) restrict the negotiation of issued shares; ii) require prior authorisation of the shareholders' assembly for the transfer of shares; iii) set out grounds for exclusion of shareholders; and iv) establish arbitration or amicable composition agreement for the resolution of corporate conflicts. The conversion of the company into any other type of corporate structure also requires the unanimous approval of the shareholders.

Corporations (S.A.), on the other hand, require a qualified majority for decisions such as: i) distribution of profits (at least 78% of the shares represented at the meeting); ii) issuance of shares without the pre-emptive right (70% of the shares

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represented at the meeting); and iii) payment of dividends in shares (80% of the shares represented at the assembly).

The board of directors may meet as agreed in the by-laws and its decisions will be made in line with the affirmative vote of the majority of its members. However, qualified majorities may be established in the by-laws.

The general managers or legal representatives of a company make business decisions following the policies established by the board of directors or by the shareholders. Under Colombian law, the general manager or other officers who are appointed as legal representatives under the by-laws, represent the company and are able to sign binding documents.

4. Directors and Officers

4.1 Board Structure

Corporations (S.A.) must have a board of directors. However, simplified stock corporations (S.A.S.) and limited liability companies (Ltdas) do not have to have a board of directors. For companies whose shares are not publicly traded, there are no legal requirements related to the structure of the board of directors, other than those set out in **4.3 Board Composition Requirements/Recommendations**. The requirements for companies whose shares are publicly traded are set out in **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**. A president and a secretary are typically selected to lead and record the decisions taken in the board meetings. The appointment of independent members is not mandatory for unlisted companies. However, it is becoming more common.

4.2 Roles of Board Members

The board of directors are considered administrators and form a collegiate body of the company. However, as directors, they cannot represent the company (unless they are granted a power of attorney by the legal representative). The legal representative is the officer of the company who represents it and can bind it with their signature and any delegation of authority must come from the legal representative, even if authorised by the board.

The board of directors is an advisory and collaborative body, which is empowered to order the execution or performance of certain acts or agreements. It can take particular decisions to enable the company to fulfil its corporate purpose and is usually in charge of the company's policies.

4.3 Board Composition Requirements/Recommendations

Corporations must have a board of directors. The board must consist of at least three members with replacements specified. Directors must be individuals and cannot be companies. There are no residency or nationality requirements for members.

4.4 Appointment and Removal of Directors/Officers

The members of a board of directors are appointed and removed by the shareholders' assembly. The managers (legal representatives) are appointed by the board of directors or by the shareholders' assembly.

The appointment of directors and legal representatives of a local vehicle must be registered at the Trade Register. For these purposes, the minutes/resolutions (ie, shareholders' or board resolution) appointing the directors and officers,

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must be filed with the letter of acceptance and a copy of the appointed person's identification document.

The appointment of the officers will be effective upon their registration at the Trade Register. The members of the board of directors can act as officers if this is accepted. They can do so even if their appointment has not been registered with the Trade Register if their decisions do not require public registration. Legal representatives must obtain a personal tax ID and update the company's tax ID information.

4.5 Rules/Requirements Concerning Independence of Directors

The appointment of independent members is not mandatory for unlisted companies. However, it is becoming more common. Provision for this can be made in the company's by-laws. Directors and officers should abstain from engaging directly or indirectly in their own interests or the interests of third parties in activities involving competition with the company or acts involving a conflict of interest, unless prior written authorisation has been provided by the shareholders' assembly and is therefore not harmful to the company.

4.6 Legal Duties of Directors/Officers

The law lists the duties that apply to administrators which include:

- making all efforts to adequately develop the corporate purpose;
- ensuring that the laws, by-laws and duties are strictly complied with;
- ensuring that the instructions of the statutory auditor are carried out; and
- confidential commercial and industrial information is protected.

Administrators are required to act in good faith and with due care and loyalty. They are also required to meet the standard of a good businessman. There is a presumption that in making a business decision, the directors of a company acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.

However, corporate administrators enjoy full autonomy when making business decisions and are protected from being held personally liable as long as the decisions do not contravene legal and statutory provisions. This autonomy is commonly known as the business judgement rule.

A company is bound by the acts of officers to the extent that these fall within the powers granted to them under the by-laws of the company and provided that they fall within the corporate purpose of the company.

4.7 Responsibility/Accountability of Directors

Directors must exercise their duties in good faith, with loyalty and with the diligence of a good businessman. They will act in the interests of the company and take the interests of shareholders into account. Directors will be jointly and unlimitedly liable for any damage they may cause to the company, its shareholders or to third parties because of fraud or negligence.

4.8 Consequences and Enforcement of Breach of Directors' Duties

The mechanism established by law for directors to repair the damage to the company is known as the company responsibility action (*acción social de responsabilidad*). This is valid in the cases where directors may have caused damage to the company, the shareholders or to third parties, in the performance of their duties because

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of fault or fraud. This action will be initiated by the company, after a decision of the shareholders' assembly or the partners' meeting.

When the shareholders' assembly has decided to initiate this action but it has not started it within the following three months, it may be initiated by any director, the statutory auditor or any of the shareholders in the best interest of the company.

Creditors representing at least 50% of the company's external liabilities may also initiate the action as long as the company's assets are insufficient to satisfy their claims.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

The company's by-laws may establish other types of sanctions for directors who fail to perform their duties. It is not possible to absolve or limit the liability of the directors. Any clause that goes against this provision is considered unwritten. D&O insurance can be arranged to cover certain risks.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Any decision related to the remuneration of directors and officers must be approved by the shareholders' assembly or the company's board, as applicable. A legal representative or director must disclose any conflict of interest in matters involving remuneration, fees or other benefits.

Failure to do so means that the director or officer could be investigated for not disclosing the conflict of interest and the decision on the salary could be void. The director or officer must also indemnify against any damage caused.

4.11 Disclosure of Payments to Directors/Officers

According to Article 446 of the Commercial Code, the board of directors must prepare a report including details of expenditures for salaries, fees, representation expenses, bonuses, benefits in cash and in kind, transportation expenses and any other type of remuneration received by each of the company's officers. This report is presented at the shareholders' assembly.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Shareholders are the "owners" of the company. Their main role is to make a capital contribution to the company (either in kind or in cash) in return for a participation percentage in the company (shares or quotas), which will allow the entity to start its productive activity, in order to obtain profits that allow a subsequent distribution of dividends to the shareholders.

The term for the payment of capital contributions and the liability of the shareholders/partners for each type of entity are as follows.

Simplified Stock Corporations (S.A.S.)

The responsibility of the shareholders is limited to the amount of their contributions, except in cases of fraud or abuse by the company which causes detriment to third parties. The capital of the company must be paid within the two years following its incorporation.

Corporations (S.A.)

At incorporation, the shareholders must subscribe at least 50% of the authorised capital and pay at least one-third of the subscribed capital.

The remaining two-thirds must be paid within a year of incorporation. Liability is limited to the capital contribution in the absence of fraud or abuse.

Limited Liability Companies (Ltdas)

The partners' responsibility is limited to the amount of the capital contribution, which must be paid in full when the company is incorporated and on any additional increase, partners are not liable for the payment of any debt, except for tax obligations or labour liabilities, for which they are severally and jointly liable with the company and share capital that has not been fully paid.

Branches of Foreign Companies

Assigned capital must be fully paid. Any increase requires authorisation of the home office's competent corporate body and registration in the Trade Register. Supplementary investment to assigned capital does not require any formalities and can generally be made in cash from abroad.

A branch does not have a separate legal personality to that of its home office. The home office is liable for the assets and liabilities of the branch in Colombia. The home office and the branch are jointly and severally liable for all business conducted in Colombia through the branch, including the tax and corporate obligations of the branch, without limitation.

In addition, the shareholders are in charge of approving by-law amendments, setting economic guidelines for the business and policies for the management of the company, starting corrective actions against the management and making decisions on the profits. These decisions are usually made following the quorum set out in the law or the by-laws for these matters.

5.2 Role of Shareholders in Company Management

Shareholders do not generally hold a managerial position solely because of their status as shareholders. However, they can be appointed to management positions as there are no legal provisions prohibiting this.

Apart from cases of legal representation, the administrators and employees of the company may not represent shares, other than their own, at the meetings of the board of partners or the shareholders' assembly of corporations or limited liability companies, while they are in office, nor may they substitute the powers conferred upon them. They may also not vote on the balance sheets and accounts at the end of the fiscal year or on the liquidation accounts.

5.3 Shareholder Meetings

The shareholders or partners must hold an annual meeting within the term set out in the by-laws. Where no provision is made, the meeting must be held within the first three months of each calendar year. The matters to be considered at the annual meeting include the:

- appointment of directors, officers and statutory auditor;
- approval of the annual management report;
- approval of the statutory auditor's opinion on the annual financial statements;
- approval of the annual financial statements; and
- approval of the project for the distribution of profits.

5.4 Shareholder Claims

The company responsibility action (*acción individual de responsabilidad*) may be initiated when acts of the administrators (members of the board of directors, officers) caused specific damage to

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third parties or to a specific shareholder (and not directly to the company) by acting in the name and on behalf of the company negligently, fraudulently or in extra limitation of their functions as administrators. The damage suffered by the party by virtue of the violation of the duty of conduct must be demonstrated and the damage caused to the personal assets of the shareholder or third party affected by the actions of the administrators must be compensated for.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Companies that wish to register in the RNVE must provide a copy of their shareholder composition and give a breakdown of the beneficial owners. All issuers must disclose significant changes to the composition of the issuer's shareholding (that is, any variation equal to or greater than 5% of the issuer's capital) which has its origin in the purchase or sale of the capital by a person or group of persons who directly or indirectly form the same beneficial owner, in a truthful, sufficient, complete and understandable way for investors and the market in general.

Publicly traded companies listed in one or more stock exchanges also have to report information on their beneficial owners to the tax authority. Any and all individuals exceeding 5% or more of ownership/economic benefit or control over the Colombian entity must be reported.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Annual financial statements must be deposited in the Trade Register of the entity's domicile or with the Superintendence of Companies (as applicable).

Entities permanently supervised or controlled by the Superintendence of Companies and entities that received a special request from the Superintendence of Companies must file financial statements with their notes, management's report, statutory auditor's opinion and minutes of the annual general meeting. If controlling companies have more than one entity in Colombia or have registered as a business group, they must also file consolidated or combined financial statements with the Superintendence of Companies.

If a business group has been registered, the companies must also file their consolidated or combined financial statements with the tax authority, according to Article 631-1 of the Tax Code.

6.2 Disclosure of Corporate Governance Arrangements

Company by-laws are registered in the Trade Register's office and are public. Corporate governance arrangements are not generally public for private companies. However, this is not so for listed companies where there is an obligation to disclose a report to investors, which should contain, among other things:

- an analysis of the corporate governance of the entity and a description of the management structure of the entity;
- compensation schemes of directors and officers;
- the composition of the board of directors and officers and backgrounds of the directors and officers;
- quorums of the meetings;
- management of conflicts of interest;
- statutory auditor's fees; and
- a description of the committees established to control internal audit processes and equity treatment.

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Companies that are supervised or controlled by the Superintendence of Companies can sign a Sustainability Report, which includes information on corporate practices and certain corporate governance matters. This new Sustainability Report option was introduced earlier in 2025 and is expected to become mandatory in the future.

6.3 Companies Registry Filings

The following filings are required and are also publicly available.

- Renewal of the commercial registration of the entity and its commercial establishments at the Trade Register.
- Renewal of the public contracting register.
- Documents of incorporation of a company or branch and any amendments.
- Appointment of administrators (legal representatives, members of the board of directors, statutory auditors and liquidators).
- Appointment of general powers of attorney granted by the company.
- Dissolution and liquidation of companies.
- Capital increases and reductions.
- Mergers and demergers.
- Global transfers of assets: where the company intends to dispose of assets and liabilities that represent 50% or more of the company's liquid assets.

Failure to register these documents makes them unenforceable against third parties.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

If the entity's assets or gross income were more than 3.000 (approximately USD975,000) and 5.000 (approximately USD1,650,000) minimum monthly wages in the previous financial year, it

must appoint a statutory auditor. The statutory auditor must be a Colombian public accountant and must meet the independence provisions. The following persons cannot be appointed as statutory auditors.

- Shareholders from the company, its parent company or any of its subsidiaries.
- Employees from the parent company.
- Those who are related by marriage or kinship up to the fourth degree or first or second degree.
- Those who are administrators' partners and executive officers such as the cashier, auditor or comptroller of the company.
- Those who hold any other position in the same company or its subsidiaries.

Elected statutory auditors may not hold any other position in the company or in its subsidiaries during the same period.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Directors and legal representatives must ensure that the accountant keeps the company books and that statutory auditors are allowed to properly perform their functions.

They must implement a money laundering, financing of terrorism and financing of proliferation of weapons of mass destruction integral risk management and self-control system when the annual total assets or gross income exceed specific thresholds according to a company's industry.

Likewise, a transparency and business ethics programme must be adopted when certain international transactions or contracts with state bodies exceed specific thresholds.

Trends and Developments

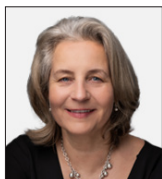
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Baker McKenzie

Baker McKenzie has been present in Colombia for 80 years and is a leading figure in the legal landscape of South America. Its office in Bogotá works on cross-border transactions with the Baker McKenzie network in the region and across the globe, primarily with the London office as well as the New York, Chicago, Houston and West Coast offices in the US, seamlessly supplying its clients with relevant and effective advice. It assists national and multinational

companies with the legal needs of their businesses in the country and abroad. Having acted in some of the country's largest transactions and projects, it is recognised as one of the top legal advisers in the country. It has global capabilities and an instinctively global mindset which gives it the ability to embrace complexity across boundaries with pragmatism, ease and sophistication. Being global is really a part of its DNA and has been its defining focus.

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Increased Focus of Colombian Authorities on Corporate Governance

Over the last few years, the regulatory landscape for corporate governance in Colombia has undergone significant transformation. While regulations and guidelines on information transparency and good business practices have existed for over 50 years in some cases, the authorities and regulatory bodies have intensified efforts to educate the business community and enforce the existing rules.

They have recently introduced new regulations on identifying final beneficiaries, regulating conflicts of interest and preparing sustainability reports. The increased scrutiny on transparent business practices, climate change and environmental, social and governance (ESG) has placed corporate governance centre stage in Colombia.

Corporate governance is no longer regarded as exclusively applicable to publicly traded companies. Large private companies and subsidiaries of multinationals are increasingly implementing more robust governance rules to drive profitability and innovation as well as attract investment and align with the interests of stakeholders. All entities, even small and micro-sized businesses have to identify and register final beneficiaries with the Colombian tax authorities.

They also often have to identify and register final beneficiaries with third-party customers and suppliers even if they usually fall under revenue and asset thresholds for mandatory reporting in other areas.

Corporate governance is slowly being regarded less as a set of onerous, expensive and irrelevant rules transplanted from other jurisdictions and is instead being viewed more and more as a mechanism for succession planning. With

approximately half of registered entities being family companies in Colombia, improved professional standards are required for management bodies and monitoring by investors. For these companies, the challenge is striking the right balance between the potential benefits in the mid to long-term of adopting these policies and the costs and administrative burdens involved.

Some of these measures and their effects on the Colombian business environment are discussed below.

Greater Transparency *Registry of Ultimate Beneficial Owners*

Regulations requiring all companies and entities to register the individuals qualifying as ultimate beneficial owners (UBOs) by 31 July 2023 came into force in 2021. New entities must register qualifying individuals within two months of incorporation. There are two main criteria for identifying individuals as UBOs:

- ownership criteria: direct or indirect owners of 5% or more of the capital or voting rights, assets, benefits or profits of the entity; and
- control criteria: direct or indirect control over the entity other than by ownership.

Where no UBOs are identified under these criteria, the legal representative of the entity must be registered unless there is someone with a position of greater authority in relation to the management functions and administration of the entity. If this is the case that person must be identified instead. There is no exception for final parents that are publicly traded nor for foreign individuals identified as UBOs.

The registration must be made electronically on the platform of the Colombian tax authorities (DIAN). Registration is expected to be an impor-

tant tool in preventing tax evasion, money laundering, financing of terrorism, corruption, transnational bribery and illegal collection of funds. DIAN has started following up with entities that have not yet registered in the UBO register.

The adoption of these measures is consistent with emerging global trends in Europe, Asia and the United States. For companies interested in attracting foreign investors, new regulations in these jurisdictions (along with vigilant government review), will allow for better informed judgements and confidence when engaging in foreign financial transactions and due diligence.

Disclosure of business groups

The registration of UBOs with the Colombian tax authorities should also be consistent with corporate registrations required of Colombian entities at the public trade register. The disclosure of business groups and control situations in this register has been mandatory since the enforcement of Law No 222 of 1995.

In the last few years, the Superintendence of Companies, the regulator for companies whose shares are not publicly traded or subject to supervision by other Superintendencies, has specified the level of detail that must be disclosed on the ownership chain up to the final parent or controlling entity.

It issued regulations granting a period during which companies could update their ownership chain voluntarily to comply with the directions issued by the Superintendence of Companies on disclosing accurate and complete information in exchange for reduced fines in 2021.

This measure has created an environment where companies must be accurate and detailed in disclosing their control structures, ensuring that

all information on their control chain is properly registered. Failure to do so is becoming easier to detect and sanction given the different transparency measures in both Colombia and abroad. There have been several high-profile cases in the last 12 months in which entities were fined by the Superintendence of Companies for not disclosing all members of registered groups or the full ownership chain.

Conflicts of interest

Another significant change in the Colombian corporate governance landscape has been the update to the conflicts of interest regime. The new provisions of Decree No 46 of 2024 make it clear that any direct or indirect interest that may compromise an administrator's judgement or independence in making decisions in a company's best interest must be disclosed to shareholders. Administrators include board members, legal representatives and liquidators, among others.

Decree No 46 of 2024 also provides a comprehensive guide to the procedure for disclosing this conflict of interest and obtaining authorisation from the shareholders to carry out the transactions. Endorsement by investors may be granted as long as the proposed business or activity does not harm the company's interest.

Additionally, to avoid abusive related party transactions, new provisions establish that there is a conflict of interest for administrators when contracting with the company's direct or indirect controlling entity or any of their subsidiaries.

The other focus of attention has been to hold administrators accountable for their actions. When controlling shareholders are directly involved in the company's management or have delegated this function to a person close to

them, the reality is that it is not feasible to bring legal actions against directors or legal representatives on behalf of the company for breaching their duties in order to obtain compensation. In response to this legal loophole, new provisions have introduced a derivative action for shareholders to make claims for damages caused to a company resulting from directors' infringing their legal duties.

These measures aim to ensure that decisions made by administrators are in the company's best interest. By establishing clear and strict rules on how to handle conflicts of interest, the authorities seek to foster a culture of integrity and responsibility in business management. This greater corporate transparency also enhances minority investor protection placing Colombia as an economy in line with best corporate governance practices.

In December 2024, a draft bill was presented to the Colombian Chamber of Representatives to update existing corporate regulations. It proposes introducing new rules on administrators' duties, liabilities and conflicts of interest. It defines conflicts of interest, related parties, acts that imply competition with the company and usurpation of corporate opportunities more broadly, when compared with the definitions that currently exist in Decree 46 of 2024.

Under the draft bill, directors' fiduciary duties could be extended to any shareholders with a personal interest in a particular transaction under the conflict of interest rules where the company suffers damage.

ESG

Sustainability reports

Despite changes in global trends towards sustainability in some jurisdictions, Colombian

regulators retain their focus on sustainability. The Superintendence of Companies introduced guidelines on a new Sustainability Report in March 2025 in addition to the existing Chapter XV of the Basic Legal Circular Letter containing recommendations for unlisted companies to report the effects of their activities in various areas of sustainability such as the environment, society and inclusion.

These recommendations, which are still voluntary, promote the implementation of international standards and practices aimed at improving the competitiveness of companies. The intention, as indicated by the Superintendence of Companies in multiple academic settings, is that eventually, entities meeting certain requirements must implement and launch a Sustainability Programme and report to the Superintendence of Companies.

Entities subject to permanent supervision by the Superintendence of Companies with assets or income in the previous financial year exceeding approximately USD13 million fall within the scope of these regulations and will have to file this information in the future as will entities engaged in certain activities in the mining and energy, manufacture, construction, tourism, telecommunications and new technologies sectors when they generate income exceeding approximately USD9.7 million.

For the 2025 corporate filings, the Superintendence of Companies issued guidelines on the submission of "*Non-Financial Information*" for unlisted companies, creating a new report on sustainability which includes a section on governance and business practices. Although it is optional to file this report in 2025, it is likely to become mandatory in the near future.

Listed entities are required to disclose information on social and environmental issues, including climate issues. The mandatory annual report includes items such as:

- sustainability and responsible investment practices applied;
- environmental and social metrics under international standards;
- actions implemented to achieve social objectives; and
- an explanation on how they achieve social and environmental matters when they include these matters in their advertising.

Quarterly reports on any material change to these practices and processes are also required.

Due diligence

ESG factors continue to play an important role in M&A and corporate-related processes. Investors are prioritising due diligence on ESG matters to ensure that potential targets align with their own ESG values, have sustainable business models and are not exposed to significant reputational risks. For example, due diligence on environmental, human rights issues, displacement and protection of communities in property transactions and infrastructure projects is becoming more common in transactions in Colombia.

As ESG policies and regulations are established around the world, multi-jurisdictional transactions inevitably become subject to global expectations for representations and warranties, thereby affecting purchase price, indemnity obligations and other transaction terms. Even when evaluating the attractiveness of an investment, the adoption of, and compliance, with ESG policies and regulations is an important factor when determining operational and cultural fit.

The promotion and inclusion of international standards in sustainability and corporate governance therefore means that Colombian companies will likely be held to global practices and standards. By embracing the trend, companies will therefore not only align with the best international practices that continue to exist in many foreign jurisdictions but may also open doors in foreign markets, improve global competitiveness and make Colombian companies more attractive targets for foreign investment.

Corporate governance

The relevance of a transparent and robust corporate governance regime for investors has focused businesses on regulating relationships between shareholders, directors, management and other stakeholders. Rules on shareholder rights, accessibility to information and equality of treatment for shareholders are common among large unlisted companies.

Independence and diversity on boards

While publicly traded companies must have independent members making up to 25% of the board by law and majority state-owned publicly traded companies must have 30% of the board made up of female members, private companies are also seeking independent members and greater diversity among skill sets, age, gender and race. For example, organisations such as the 30% Club and the Programme for Female Board Members of the CESA University (which currently has more than 700 graduates) have focused on the benefits of gender diversity, monitoring advances and leading upskilling programmes for female executives.

Female board membership in Colombia has increased from 15% in 2015 to more than 25% in 2025 according to the National Securities Register of the Financial Superintendence. Train-

ing and evaluation of board members, preparation of board regulations setting out policies on conflicts of interest, remuneration and functions and responsibilities are being adopted voluntarily by larger and mid-sized companies:

- to regulate relationships between the different stakeholders better; and
- to drive profitability and succession planning in second and third generation companies.

Diverse boards globally are often viewed as being able to make decisions more effectively and approach strategy and risk from a broader perspective. In fact, board diversity can help validate and evidence actions taken in good faith under the newly adopted business judgement rule in Colombia. It can also be used to justify any waivers of conflicts of interest, as the directors without any direct interest can still analyse the issue as being in the best interest of the company.

Additionally, for businesses to expand and remain competitive in a multinational environment, boards should have an understanding of their diverse customer base, shareholders and other stakeholders.

Audit committees and statutory auditors

Publicly traded companies in Colombia must have an audit committee made up of three directors, including directors who are considered to be “*independent*”. This committee is responsible for monitoring compliance with the internal audit programme and for guaranteeing that financial information is prepared in line with legal requirements.

All committee meetings must be attended by the company’s statutory auditor, who might be able to deliver opinions on the matters under discus-

sion. Auditing and ethics committees are also common amongst private companies and non-profit entities to provide guidance to the board.

The role of the statutory auditor has long been to supervise proper accounting records and ensure that the company’s activities are performed in compliance with the by-laws and board and shareholder decisions, among other duties. This role has been expanded over the last few years to cover other matters such as reviewing and reporting on anti-money laundering and business transparency programmes, reporting on suspicious operations to the relevant anti-money laundering authorities and alerting the shareholders to any acts of unfair competition and conflicts of interest. Auditors are being held to account by the authorities to review and issue formal opinions on these matters, even for private companies, where applicable.

Business judgement rule

New regulations expressly accept the application of the business judgement rule, which has been widely recognised by local case law. This will encourage management to make decisions that will require taking greater risks but could also mean higher economic returns without the fear of being prosecuted later. Therefore, as long as directors are acting in good faith, are duly informed, are acting rationally and within the authority established by law and the by-laws, courts should not review or question their decisions.

The business judgement rule was recently extended to all authorities in Colombia as part of a major innovation to provisions on the matter.

Enforcement

Government agencies have recently become more active in enforcing transparency and

governance obligations. In April 2024, an inter-administrative agreement was signed between the Superintendence of Companies and DIAN to share information reported by entities in the last year on the register of ultimate beneficial owners. The agreement was aimed at starting administrative investigations to determine individuals with decision-making power over companies as well as enhance the control over money laundering, international bribery and responsibility in corruption schemes.

The Superintendence of Companies has generally taken a much more active role in holding administrators of Colombian entities to account for compliance with their legal and statutory obligations as well as the statutory auditors for failing to monitor and report on deficiencies. In recent years, numerous investigations of companies, their administrators and auditors have resulted in significant sanctions for those who have failed to comply with their responsibilities.

These sanctions not only have a direct economic impact but also send a clear message to the business community about the importance of adhering to proper corporate governance practices. The investigations have highlighted cases involving lack of transparency, failure to disclose conflicts of interest, failure to prepare and give access to financial statements and failure to provide timely and accurate information to shareholders and other irregularities that might have previously gone unnoticed.

This increased level of involvement by the Superintendence of Companies has created an expectation that companies and their administrators and auditors must be more diligent and proactive in their governance practices and plan and implement improvements to avoid delays in meeting tight corporate filing deadlines.

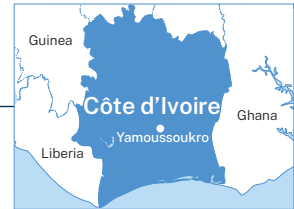
Conclusion

The increased focus of Colombian authorities on corporate governance reflects a global trend towards greater transparency and accountability in business management. The measures implemented by the Superintendence of Companies, DIAN and other regulatory entities aim to ensure that Colombian entities operate ethically and transparently, fostering a more reliable and competitive business environment.

While these changes present significant challenges for companies in terms of compliance costs and adaptation to new regulations, they also offer opportunities to improve transparency, accountability and competitiveness. By adopting these best practices, companies will not only avoid sanctions but will also have the chance to strengthen their market position and gain the trust of investors while promoting diversification of funding sources and therefore more dynamic capital markets.

In this context, it is crucial for Colombian entities to take corporate governance seriously and strive to comply with established regulations. There are still a significant number of chief executive officers and directors of boards with very limited knowledge of corporate governance. Transparency and accountability are not only regulatory imperatives but also key factors in the long-term success and sustainability of any organisation. Companies that adopt these principles will be better placed to thrive in an increasingly demanding and competitive environment.

CÔTE D'IVOIRE



Law and Practice

Contributed by:

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Houda Law Firm is a multi-sectoral and multi-disciplinary law firm based in Senegal and Côte d'Ivoire. The firm has a total staff of 53 people, comprising a team of lawyers, jurists and paralegals. The staff work in French and English to ensure the satisfaction of local and international clients. Houda Law Firm provides legal advice and assistance to a diverse clientele in

a variety of practice areas, including business law, insurance law, banking and finance, public and private international law, contract law, mining, oil and gas, renewable energy, and tax. The firm has proven expertise in the energy and extractive sector, as well as in PPPs, banking and finance, and corporate and commercial law.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Commercial companies are governed in Côte d'Ivoire by the Uniform Act on Commercial Companies and Economic Interest Groups (*Acte Uniforme révisé relatif au droit des Sociétés Commerciales et du Groupement d'Intérêt Économique*, or AUSCGIE), published on 30 January 2014. The most commonly used commercial forms are, in order, the *société à responsabilité limitée* (SARL), the *société anonyme* (SA) and the *société par actions simplifiée* (SAS). In Côte d'Ivoire, the creation of an SA or an SAS requires recourse to a notary public.

SARL

The SARL is the simplest form of commercial company, in which the liability of the shareholders is limited to contributions. The SARL may be established by one natural or legal person or between two or more natural or legal persons. The amount of capital is freely determined by the partners in the articles of association and is divided into shares with a nominal value of not less than XOF5,000.

The SARL is often characterised by a fairly strong *intuitu personae*, which is why transfers of shares are often governed by specific authorisation rules given by the non-transferring shareholder. The SARL is managed by one or more natural persons, associated or not.

In addition, the SARL is not required to appoint an auditor unless it meets two of the following conditions at the end of the financial year:

- a balance sheet total exceeding XOF125 million;
- an annual turnover exceeding XOF250 million; and/or
- a permanent staff of more than 50 persons.

The partners in the SARL meet in a general meeting, either ordinary (each year for the approval of the accounts of the closed financial year, the appointment or dismissal of managers, and – more generally – to decide on all matters that do not require amendment of the articles of association) or extraordinary (for any decision involving a change in the articles of association).

The SARL is a suitable corporate structure for greenfield projects, commercial activities and

services. It is also suitable for young entrepreneurs with few resources, owing to its low formation cost.

SA

The SA is a company in which shareholders are only liable for the company's debts up to the amount of their contributions. Shareholders' ownership rights are represented by shares.

The minimum share capital of an SA is XOF10 million. It must be fully subscribed by the shareholders and at least one quarter of the total share capital must be paid up at the time of incorporation and the remainder must be paid up within three years.

The SA under the AUSCGIe, may be held by a single shareholder. In terms of management and administration, the founder(s) must choose unequivocally in the articles of association between:

- an SA with a board of directors (one shareholder or more); or
- an SA with a general manager (up to three shareholders).

The founders of an SA must appoint a statutory auditor and an alternate auditor, chosen from among experts who are members of the Order of Chartered Accountants of Côte d'Ivoire (Article 695 of AUSCGIe).

SA with a board of directors

The board of directors is composed of a minimum of three persons and a maximum of 12 members, shareholders or not. The articles of association may require each director to own a number of shares of the company over which they preside. It is possible to appoint corporate directors, who appoint a permanent representative to the board.

The board appoints the chair of the board of directors from among the natural persons who are members of the board and also appoints the CEO of the company, who may be one third of the board. It may also be decided to appoint a chair and CEO who will combine both roles.

The board of directors determines the company's strategic objectives and ensures their implementation. It controls and verifies the proper functioning of the company and settles matters regarding the company through its deliberations. The chair of the board of directors presides over board meetings and general meetings. The chair must ensure that the board assumes control of the management of the company, which is entrusted to the CEO under the board's oversight.

The CEO is responsible for the general management of the company and represents the company in its relations with third parties. At the suggestion of the CEO or the chair/CEO, the board of directors may appoint one or more individuals to assist the CEO or the chair/CEO as deputy CEO.

SA with a general manager (administrateur général)

The general manager assumes responsibility for the administration and general management of the company. They represent it in its relations with third parties and convene and chair the general meetings of shareholders. The general manager is vested with the broadest powers to act in all circumstances on behalf of the company but must exercise these powers within the limits of the corporate purpose and subject to those powers expressly attributed to shareholders' meetings by the AUSCGIe, and, where applicable, by the articles of association.

At the suggestion of the general manager, the general meeting may mandate one or more deputy general manager(s) to assist the director, as well as to decide other powers delegated to the deputy general manager.

The SA is a suitable form of company for the establishment of joint ventures, for companies with significant investments to make, and for companies engaged in regulated banking or financial activities.

SAS

Introduced in the AUSCGIE, in 2014, the SAS is a company set up by one or more shareholders where the articles of association determines the organisation and operation of the company, subject to certain mandatory rules (eg, competence of the shareholders' general meeting to approve the accounts or amend the articles of association).

The liability of the shareholders is limited to the contributions and there is no minimum share capital required to create an SAS. When created by a single shareholder, it is called a single-person simplified joint stock company (*société par actions simplifiée unipersonnelle*, or SASU).

The company is represented by a chairperson, appointed under the conditions provided for in the articles of association. The chairperson is vested with the broadest powers to act on behalf of the company within the limits of the corporate purpose.

The articles of association freely determines the decisions that must be taken collectively by the shareholders and stipulate the conditions and forms in which the shareholders must take these decisions. Decisions taken in violation of the statutory clauses are null and void.

The appointment of one or more auditors is optional unless the SAS meets two of the following conditions at the end of the financial year:

- a balance sheet total exceeding XOF125 million;
- an annual turnover exceeding XOF250 million; and/or
- a permanent workforce of more than 50 people.

An SAS that controls or is controlled by one or more companies is also required to appoint at least one auditor.

This form of commercial company is appropriate for companies with diverse shareholder profiles – ie, particularly where investors and project leaders, equity companies, and companies operating in the field of services and new technologies are among the company's shareholders.

1.2 Sources of Corporate Governance Requirements

As Côte d'Ivoire is a member state of the Organisation for the Harmonisation of Business Law in Africa (*Organisation pour l'Harmonisation en Afrique du Droit des Affaires*, or OHADA), company law in Côte d'Ivoire is subject to OHADA law – more specifically, to the AUSCGIE. The articles of association and the shareholders' agreement are also sources of corporate governance.

Ivorian law can also be a source of corporate governance requirements for companies, provided that it complements rather than contradicts OHADA laws.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies making a public offering of their shares in one or more OHADA contracting states or whose shares are listed on the stock exchange of one or more OHADA contracting states are required to have a board of directors. The boards of directors of the companies must be composed of at least three members and at most 15 members at the time a company's shares are admitted to the stock exchange.

However, in the event of a merger involving one or more companies whose shares are admitted to the stock exchange of one or more “*state parties*”, the number of members may exceed 15 (up to the total number of directors who have been in office for more than six months in the merged companies) but may not exceed 20. When the shares of the company are admitted to the stock exchange of one or more of the party states, no new directors may be appointed – nor may directors who have died or ceased to hold office be replaced – until the number of directors has been reduced to 15. If a company admitted to the stock exchange of one or more state parties is delisted from that stock exchange, the number of directors must be reduced to 12 as soon as possible.

Within the various limits set out here, the number of directors is freely determined in the articles of association.

The board of directors of the company is obliged to have an audit committee (*comité d'audit*). The audit committee is composed exclusively of directors who are not employees of the company or who do not hold a position as chair/CEO, CEO or deputy CEO within the company. The board of

directors ensures the competence of the directors it appoints to the audit committee.

The main tasks of the audit committee are to:

- review the accounts and ensure the relevance and consistency of the accounting methods used to prepare the company's consolidated and parent-company financial statements;
- monitor the process of preparing financial information;
- monitor the effectiveness of internal control and risk management systems;
- issue an opinion on the auditors proposed for appointment by the general meeting; and
- report regularly to the board of directors on the performance of its duties and inform the board of directors without delay of any difficulties encountered.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

No specific hot topics in the area of corporate governance have been identified in Côte d'Ivoire.

2.2 ESG Considerations

There are no regulations on ESG issues in OHADA law. These provisions will, for example, be provided for by the board of directors or provided for by the internal regulations on a case-by-case basis for companies that can draw on international regulations in this area.

Ivorian law, if enacted, can also be a source of ESG requirements for companies. However, it must not be in conflict with OHADA laws.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

In general, in commercial companies:

- the management body, the officers, and the board have – within the time limits set forth in the AUSCGle, for each type of company – full powers to bind the company towards third parties without having to produce a special power of attorney and any limitations on their legal powers by the articles of association will be unenforceable against bona fide third parties; and
- the company is bound by acts of its management body, its officers and its board that are not within the company purpose, unless the company can prove that the third party was aware that the act was unrelated to that purpose or could not ignore this given the circumstances – although the mere publication of the articles of association is not enough to prove it.

SARL Management

A SARL is managed by one or more managers (*gérants*), who must be natural persons. Managers may or may not be shareholders of the company. The managers are appointed by the shareholders in the articles of association or by a decision of the shareholders' general meeting. In the absence of specific provisions in the articles of association, the manager(s) is (are) appointed for four years and are re-eligible. There are no nationality or residence requirements for managers.

SA Management

The articles of association must specify under which of the following management structures the SA will be managed:

- a board of directors with a single chairperson and general manager (*président-directeur général*), who must be a director of the company and a natural person; or
- a board of directors with a chairperson of the board and a separate general manager (*directeur général*), who must be a natural person but does not have to be a director of the company and who may be assisted by one or more assistant general managers.

In both of these scenarios, directors may or may not be shareholders of the company, unless provided for in the articles of association. The board must have at least three and no more than 12 directors.

Companies having fewer than three shareholders may choose not to form a board of directors and instead to appoint a general manager (*administrateur général*, who may or may not be a shareholder of the company) who will be responsible for the administration and direction of the company.

SAS Management

An SAS is represented towards third parties by a president, who may be a natural or legal person and who may or may not be a shareholder of the company. The articles of association may provide for the conditions under which one or more individuals other than the president, with the title of general manager or deputy general manager, may exercise the powers entrusted to them by the articles of association. Restrictions on the powers of the president, general manager or deputy general manager, as detailed in the provisions of the articles of association and the decisions of legal representatives, are not enforceable against third parties.

It is also possible for an SAS to set up a board of directors.

3.2 Decisions Made by Particular Bodies SARL Decision-Making

In relation to the shareholders and in the absence of determination of the manager's powers by the articles of association, the manager may carry out all acts of management in the interest of the company. Where there is more than one manager, they shall hold separately the powers provided for in the articles of association, except for the right of each of them to object to any transaction before it is concluded. Opposition by one manager to the acts of another manager is without effect with regard to third parties, unless it is established that the third parties have knowledge of it.

SA Decision-Making

SA with a board of directors

The board of directors determines the SA's strategic objectives and ensures their implementation. Within the limits of the company's purpose and subject to any decision-making powers expressly delegated to the shareholders' meetings, the board of directors deals with any issue concerning the proper operation of the company and – through the board members' deliberations – settles matters that concern the SA.

The board of directors carries out any such controls and verifications as it deems appropriate. The board of directors may entrust one or more of its members with special mandates for one or more specific purposes.

The chairperson of the board of directors chairs the meetings of the board of directors and the general assemblies. The chairperson must ensure that the board of directors assumes the control of the management of the company,

which is entrusted to the general manager. At any time, the chairperson of the board of directors may carry out the verifications the chairperson deems appropriate and may obtain from the general manager – who is obliged to comply – all the documents the chairperson deems useful for the accomplishment of that purpose.

The general manager is responsible for the general management of the company. They represent the company in its relations with third parties.

SA with a general manager

The general manager is responsible for the administration and general management of the company. They represent the company in its relations with third parties, and convene and chair the shareholders' meetings. The general manager is vested with the broadest powers to act in all circumstances in the name of the company but must exercise them within the limits of the corporate purpose and subject to those powers expressly conferred on shareholders' meetings by the AUSCGle, and, where applicable, by the articles of association.

Meetings in the SA

Extraordinary general meeting

The extraordinary general meeting is the only body empowered to modify the statutes in all their provisions. The extraordinary general meeting is also competent to:

- authorise mergers, demergers, transformations and partial contributions of assets;
- transfer the registered office to any other city of the OHADA contracting state where it is located or to the territory of another state; and
- dissolve the company early or extend its term (see **5.3 Shareholder Meetings**).

Special meeting

The special meeting brings together the holders of shares of a given category. The special meeting approves or disapproves the decisions of the general meetings when these decisions modify the rights of its members.

Ordinary general meeting

The ordinary general meeting takes all decisions other than those expressly reserved for extraordinary general meetings and those reserved for special meetings (see **5.2 Role of Shareholders in Company Management**).

SAS Decision-Making

The SAS is a company set up by one or more shareholders and whose articles of association freely provides for the organisation and operation of the company. The company is represented with regard to third parties by a president appointed under the conditions provided for by the articles of association. The president is vested with the broadest powers to act in all circumstances on behalf of the company, within the limits of the corporate purpose. The articles of association may provide for the conditions under which one or more persons other than the president, bearing the title of chief executive officer or deputy chief executive officer, may exercise the powers conferred on the latter by the articles of association.

The articles of association determines the decisions that must be taken collectively by the shareholders and stipulate the forms and conditions in which the decisions must be taken. However, the powers vested in the extraordinary and ordinary general meetings of joint stock companies are – under the conditions stipulated by the articles of association – exercised collectively by the shareholders in matters of:

- increase, amortisation or reduction of capital;
- merger;
- demerger;
- partial contribution of assets;
- dissolution;
- transformation into a company of another form;
- appointment of auditors;
- annual accounts; and
- profits.

3.3 Decision-Making Processes

Decisions are taken by general meetings, which may be ordinary or extraordinary, and which decide according to the majority and quorum rules set out in the AUSCGIe, or – in the case of the SAS – in the articles of association. These rules differ according to the corporate form (see **5.3 Shareholder Meetings** for the majority and the type of decision). The general meetings are convened by the corporate representatives, following a formal procedure prescribed by the AUSCGIe.

The shareholders are convened at least 15 days before the meeting by hand-delivered letter against a receipt, or by registered letter with a request for acknowledgement of receipt, or by fax or email. The notice of meeting indicates the date, place and agenda of the meeting. The meeting cannot deliberate on a question that is not registered on its agenda.

These decisions of the shareholders must be recorded in the minutes, which indicate the date and the place of the meeting, the names and first names of the shareholders present, the agenda, the documents and reports submitted for discussion, a summary of the debates, the text of the resolutions put to the vote, and the results of the votes.

4. Directors and Officers

4.1 Board Structure

An SA may be managed by a board of directors consisting of at least three and not more than 12 members, who may or may not be shareholders. The articles of association may require that each director own a number of shares in the company for which they make determinations. This provision shall not apply in the case of employees appointed as directors. Every director must, on the day of their appointment, hold the number of shares required by the articles of association or during their term of office.

In the case of an infringement, the director must resign from their office within three months of their appointment or - if the infringement occurs during their term of office – within three months of the date of the transfer of shares giving rise to the infringement. At the end of this period, the director shall be deemed to have resigned from their mandate and must return the remuneration received (in whatever form) without the validity of the deliberations in which they took part being called into question.

The auditors exercise a supervisory role and must disclose any violations in their report to the annual general meeting. The first directors are appointed by the articles of association or, where appropriate, by the constituent general meeting.

During the life of the company, the directors shall be appointed by the ordinary general meeting. However, in the event of a merger, the extraordinary general meeting may appoint new directors.

Any appointment made in violation of the provisions of the articles of association is null and void. The term of office of the directors is freely

determined by the articles of association, but may not exceed six years in the case of appointment during the life of the company and two years in the case of appointment by the articles of association or by the constituent general meeting.

4.2 Roles of Board Members

The board of directors determines the company's strategic objectives and ensures their implementation. The board of directors has a chairperson and may entrust one or more of its members with special mandates for one or more specific purposes.

4.3 Board Composition Requirements/Recommendations

The choice of directors is freely determined by the shareholders. There is no longer a quota rule to be respected between the number of shareholder and non-shareholder directors, as was the case with the pre-2014 AUSCGIE. However, the articles of association may require that each director own a number of shares of the company for which they make decisions. In practice, the composition of the board of directors often mirrors the composition of the company's shareholding.

4.4 Appointment and Removal of Directors/Officers

The directors or officers are appointed by the articles of association at the time of the company's incorporation, or during the company's life, by the general meeting. The terms of appointment, re-election, replacement and dismissal are freely determined by the articles of association. The directors may be re-elected unless the articles of association states otherwise. In an SA, the duration of office of the president and general manager is aligned with that of the directors.

The termination of the functions of the directors must be published in the commercial register.

4.5 Rules/Requirements Concerning Independence of Directors

Two mechanisms are provided for by the AUSCGIe, to prevent conflicts of interest between the company and its directors.

The Rules of Non-Cumulation of the Roles of Legal Representatives (in an SA)

For directors (in an SA with a board of directors)

Subject to certain reservations, a natural person – either directly or as a permanent representative of a legal entity director - may not simultaneously belong to more than five boards of directors of SA companies that have their registered office in the territory of the same state party. Any natural person who, upon taking up a new term of office, finds themselves in breach of this rule must resign from one of their terms of office within three months of their appointment.

For the president and general manager

No person may simultaneously hold more than three offices as president and general manager of an SA that has its registered office in the territory of the same party state.

Likewise, the role of president and general manager may not be held concurrently with more than two roles as general director or general manager of an SA that has its registered office in the territory of the same contracting state. Any natural person who, upon taking up a new term of office, finds themselves in breach of this rule must resign from one of their terms of office within three months of their appointment.

For the general director

No person may simultaneously hold more than three offices as a general director of corporations that have their headquarters in the territory of the same state party. Similarly, the office of general director may not be held concurrently with more than two offices of president and general manager or general manager of an SA which has its registered office in the territory of the same contracting state. A director who, upon taking up a new term of office, is in violation of this rule must, within three months of their appointment, resign from one of their offices.

The Procedure for Regulated Agreements (in an SARL, an SA and an SAS)

According to Article 438 of the AUSCGIe, the following agreements must be subject to prior authorisation by the board of directors of an SA:

- any agreement between the SA and one of its directors, general managers or assistant general managers;
- any agreement between a company and a shareholder who holds 10% or more of the company's capital;
- any agreement in which a director, general manager, deputy general manager or shareholder with a holding of 10% or more of the company's capital is indirectly interested or in which they deal with the company through an intermediary; and
- any agreement between a company and a business or legal entity, if one of the directors, the general manager, the assistant general manager or a shareholder holding a stake equal to or greater than 10% of the company's capital is an owner of the business or an indefinitely liable shareholder, manager, director, general manager, assistant general manager, general manager, assistant general

manager or other corporate officer of the contracting legal entity.

Similar provisions are provided for the SARL and the SA; regulated agreements must be approved by the ordinary general meeting (Articles 350 and 853-14 of the AUSCGIE).

4.6 Legal Duties of Directors/Officers

There are no specific provisions in the law. However, Article 480, Section 2 of the AUSCGIE, provides that the chairperson must ensure that the board of directors assumes control of the management of the company entrusted to the general manager. Thus, the chairperson and the board of directors each have a role.

4.7 Responsibility/Accountability of Directors

SARL Managers

The managers will be liable – individually or jointly and severally – as the case may be, to the company or to third parties, either:

- for infringements of the legal or regulatory provisions applicable to private limited companies;
- for breaches of the articles of association; or
- for faults committed in their management.

If several managers have co-operated in the same acts, the competent court determines the contributory share of each of them in the remedy of the damage (Article 330 of the AUSCGIE).

SA Directors

The directors will be individually or jointly and severally liable to the company or to third parties, either for infringements of the legal or regulatory provisions applicable to an SA, or for violations of the provisions of the articles of association, or for faults committed under their management.

Where several directors have co-operated in the same acts, the competent court will determine the contributory share of each of them in the remedy of the damage (Article 740 of the AUSCGIE).

In an SAS

The rules governing the liability of the members of the board of directors of an SA are applicable to the chairperson and the officers of an SAS (Article 853-10 of the AUSCGIE).

4.8 Consequences and Enforcement of Breach of Directors' Duties

Liability Actions

Two types of actions are provided for by the AUSCGIE.

Individual action

Pursuant to Articles 161 et seq of the AUSCGIE, third parties or shareholders may take individual action to hold a corporate officer liable for misconduct in the performance of their duties, without prejudice to the company's potential liability. If several corporate officers have participated in the same acts, they are jointly and severally liable to third parties.

This individual action is an action for damages suffered by a third party or by a shareholder, where the latter suffers a loss distinct from the loss suffered by the company, as a result of a fault committed individually or collectively by the corporate officers or directors in the exercise of their duties.

This action is brought by the person who suffers the damage.

Corporate action (action sociale) – Articles 165 et seq of the AUSCGIE

A corporate action is the action for compensation for the damage suffered by the company as a result of a fault committed by corporate officer(s) in the performance of their duties. The corporate action filed against one or several corporate officers can be initiated either by the company itself (through the other officers who are not involved) or by one or several shareholders in the case of failure of the competent bodies. The corporate action is reserved only for the shareholders holding shares on the day it is implemented and who retain the status of shareholder during the whole duration of the procedure.

In the case of a SARL, Article 331 of the AUSCGIE, provides that several shareholders may only claim compensation for the damage suffered by the company if they represent one quarter of the shareholders and one quarter of the company shares. These two conditions are cumulative. However, in the case of an SA, the shareholders can only exercise the corporate action if they represent at least one twentieth of the share capital (Article 741 of the AUSCGIE).

The individual and corporate action can be triggered and acted upon concurrently/simultaneously.

Grounds for Liability

A breach of directors' duties would give rise to their liability. Similar provisions govern the rules pertaining to the liability of corporate officers and directors in the different types of companies that have been described: SARL, SA and SAS. A distinction must be made between civil and criminal liability.

Civil liability of the manager of a SARL and the directors of an SA

The liabilities are similar for the manager of a SARL and the directors of an SA. They are liable – individually or jointly and severally, as the case may be – to the company or to third parties, either for breaches of the laws or regulations applicable to companies, or for breaches of the articles of association, or for misconduct in their management. If several managers or directors have co-operated in the same acts, the competent court will determine the contribution of each of them to the compensation for the damage.

In addition to the action for compensation for the damage suffered personally, the shareholders representing one quarter of the shareholders and one quarter of the shares may – either individually or by grouping together – proceed with the social action for liability against the manager or director(s). No clause in the articles of association may make the exercise of the corporate action subject to the prior notice or authorisation of the meeting or entail a waiver in advance of the exercise of this action.

No decision of the meeting may have the effect of extinguishing an action for liability against the managers for misconduct committed in the performance of their duties. Any decision to the contrary is null and void.

Civil liability of the CEO of an SA

The same rules of individual and social responsibility apply to the CEO.

Civil liability of the directors of an SA

Directors are individually or jointly and severally liable to the company or to third parties, either for breaches of the laws or regulations applicable to an SA, or for breaches of the provisions

of the articles of association, or for misconduct in their management.

Civil liability of the president/chairperson of an SAS

The same rules of individual and social responsibility as those mentioned for the manager and the CEO apply to the president.

Criminal liability

The AUSCGIE, contains criminal provisions in the event of offences committed by corporate officers:

- the incorporation of companies;
- the management, administration and direction of the company;
- general meetings;
- changes in the capital of an SA, capital reductions;
- company control;
- dissolution of companies;
- liquidation of companies; and
- in the event of a public offering for savings.

Law No 2017-727 of 9 November 2017 of Côte d'Ivoire describes the penalties incurred for the offences referred to in the Uniform Act. It provides for sanctions against those in control of the company, who may abuse their power or commit crimes by consciously going against the company's interest or by not following procedures and depriving the relevant parties of their rights to participate in the company's management.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other bases for claims or enforcement against directors or officers for breaches of corporate governance requirements in Côte d'Ivoire are as follows.

Management Expertise

Pursuant to Article 159 of the AUSCGIE, one or more shareholders representing at least one tenth of the share capital may - either individually or by grouping together in any form whatsoever - request the competent court of the registered office, ruling within a short period of time, to appoint one or more experts to present a report on one or more management operations.

Provisional Administration

When the normal functioning of the company is made impossible, either because of the management, executive or administrative bodies or because of the shareholders, the competent court - ruling within a short period of time - may decide to appoint a provisional administrator for the purpose of temporarily managing the company's affairs (Article 160-1 of the AUSCGIE).

Given that - according to the general law of civil liability - the potential liability of directors is likely to be implemented as soon as it can be established that they have committed errors in the performance of their duties and that these errors have had harmful consequences for the company, the shareholders or third parties, the liability of a director or officer can only be limited by proving that the damage results either from a force majeure or from a fault of the victim or of a third party.

Any clause to the contrary in the articles of association is deemed to be unwritten.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Article 325 of the AUSCGIE

In a SARL, the duties of a manager may be performed free of charge or with remuneration, under the conditions laid down in the articles of

association or in a collective decision of shareholders. The determination of the remuneration is not subject to the regime of related-party agreements.

In an SA, the ordinary general meeting may allocate to the directors - as remuneration for their activities - a fixed annual sum that it determines at its own discretion (commonly called “*jetons de présence*” in French).

Unless otherwise provided for in the articles of association, the board of directors is free to allocate the compensation among its members. The board of directors may also allocate to its members exceptional remuneration for the missions and mandates entrusted to them or authorise the reimbursement of travel expenses and expenses incurred in the interest of the company, subject to the provisions concerning regulated agreements.

A director may enter into an employment contract with the company if that contract corresponds to actual employment. Apart from sums received under an employment contract, the directors may not receive - in respect of their duties - any other remuneration (permanent or otherwise) than that provided for by the board of directors (Articles 430, 431 and 432 of the AUSCGIE).

The CEO may be bound to the company by a contract of employment. The terms and amount of the remuneration of the chairperson and general manager are fixed by the board of directors. Where necessary, the benefits in kind granted to them shall be fixed in the same manner as their remuneration. The CEO may not receive any other remuneration from the company (Article 466 of the AUSCGIE).

In the SAS, the remuneration and benefits of the chairperson and of the potential other directors are determined by the articles of association and the shareholders.

4.11 Disclosure of Payments to Directors/Officers

No public disclosure obligation in relation to the remuneration, fees or benefits payable to directors and officers for companies has been identified, except for publicly traded companies. Indeed, Article 831-2 of the AUSCGIE, requires the disclosure of the report prepared by the chairperson of the board of directors containing - in addition to the composition of the board of directors and its operating conditions - the compensation allocated to the corporate officers.

Regarding other disclosures, pursuant to Article 432 of the AUSCGIE, the exceptional remuneration of directors for missions and mandates entrusted to them - or the reimbursement of travel expenses and expenses incurred in the interest of the company - must be the subject of a special report by the auditor to the general meeting.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

A shareholder is a natural or legal person who makes a contribution (in kind, cash or industry) to the company. In return, the company delivers shares (Articles 7 and 51 of the AUSCGIE).

The status of shareholder is regulated by Articles 7 to 9 of the AUSCGIE. Those persons who cannot be shareholders are:

- any natural or legal person who is subject to a prohibition, incapacity or incompatibility provided for by a legal or regulatory provision; and
- minors and incapable adults in companies where they would be liable for the company's debts beyond their contributions.

Company shares are called "*actions*" (in French) in joint stock companies and "*parts sociales*" in other companies (Articles 7 and 51 of the AUSCGIE).

The contribution made by the shareholders determines their rights and obligations within the company:

- a right on the profits made by the company;
- a right on the net assets of the company at the time of their distribution, at the time of dissolution, or at the time of a reduction of the company's capital and intervention in the social affairs of the company;
- an obligation to contribute to the losses in certain forms of company; and
- the right to participate in the vote of shareholders' collective decisions.

The rights and obligations of the shareholders are proportional to their contribution.

In addition, according to Article 54 of the AUSCGIE, clauses that attribute to a shareholder all of the profit made by the company or exempt them from all of the losses – as well as clauses that exclude a shareholder entirely from the profit or make them responsible for all of the losses – are deemed unwritten.

Disagreement between shareholders constitutes a cause for dissolution of commercial compa-

nies within the meaning of Article 200 of the AUSCGIE.

In limited liability companies, the shareholders are only liable for the company's debts up to the amount of their contributions. The limited liability companies are:

- the SARL;
- the SAS; and
- the SA.

In the case of debts in such a company, the liability of the shareholder is limited to the loss of the total amount of their contributions in share capital and their contributions in the shareholders' current account.

Shareholders who hold management positions within the company may also be liable – individually or jointly - to the company or third parties, either for breaches of the law or the articles of association (civil or criminal liability) or for faults committed in their management.

Under OHADA law, share ownership is verified by the registration of shares in the name of the shareholder in the register of registered shares held for this purpose by the company.

5.2 Role of Shareholders in Company Management

The shareholders have a certain right of control over the management of the company, which differs according to the type of company.

SARL Shareholders

Any non-managing shareholder can, twice a year, ask the manager questions in writing about any fact that could jeopardise the continuity of the business. The manager must then provide answers within 15 days, in writing, to

the questions asked by the shareholders. Within the same time limit, they must send a copy of the questions and their answers to the auditor, if there is one (Article 157 of the AUSCGIE).

SA and SAS Shareholders

Any shareholder who does not have managerial status may, twice a year, ask questions in writing of the chairperson of the board of directors, the CEO or the general manager (as the case may be) on any fact likely to jeopardise the continuity of the business. The chairperson of the board of directors or the CEO must then reply, in writing, within 15 days, to the questions asked by the shareholder. Within the same period, they must send a copy of the questions and their answers to the auditor (Article 158 of the AUSCGIE).

The shareholder is also able to direct the actions of the corporate officers, thanks to:

- the holding of ordinary general assemblies, during which the corporate documents are controlled and approved (summary financial statements, management reports, inventories, draft resolutions, the auditor's report, and the auditor's special report on regulated agreements (if any);
- individual action (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**); and
- corporate action (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**).

5.3 Shareholder Meetings

All shareholders have the right to participate in the voting of collective decisions (Article 125 of the AUSCGIE). There are two kinds of collective decisions: ordinary decisions and extraordinary decisions (Article 132 of the AUSCGIE). These decisions can be taken within the framework of

general assemblies or by written consultation (Article 133 of the AUSCGIE). All the deliberations of the shareholders are noted by a minute (Article 134 of the AUSCGIE).

The manager is in charge of convening the general meeting. In the event of their failure to do so, the auditor may substitute for the manager. Failing this, the shareholders may request the convening of the meeting in court.

The methods of convening the meeting are set out in the articles of association. The ordinary general meeting congregates at least once a year (within six months of the end of the financial year). An extension of the deadline may be requested from the president of the competent court ruling on a petition. The purpose of the ordinary general meeting is:

- to approve the summary financial statements, the management report and the inventory (Article 140 of the AUSCGIE, for the SA, SARL and SAS) – to this end, the aforementioned documents are communicated at least 15 days before the meeting by the company directors;
- to decide on the allocation of the result (Article 142 of the AUSCGIE); and
- to determine the allocations to optional reserves, the share of profits to be distributed, and the amount of any retained earnings (Article 144 of the AUSCGIE).

In an SARL and an SA, the decisions are made by a majority of the votes present and represented.

The extraordinary general meeting takes extraordinary collective decisions (ie, decisions to amend the articles of association). It decides by

a majority of three quarters of the capital in a SARL and two thirds in an SA.

However, unanimity is required in the case of:

- an increase of the shareholders' commitments;
- transformation into an SAS; and
- transfer of the registered office to a state other than a state party to the AUSCGIE.

In the event of a loss of half of the share capital, an extraordinary general meeting must be convened within four months of the general meeting that recorded this loss, on pain of penal sanctions or request by any interested party for dissolution of the company.

In an SAS, the rules of majority and quorum are set by the articles of association.

5.4 Shareholder Claims

The bases of claim that exist for shareholders against the company or directors are as follows:

- against the company – the shareholders do not have a liability claim against the company; and
- against the directors – see **5.2 Role of Shareholders in Company Management** (social action, individual action, alert procedure).

5.5 Disclosure by Shareholders in Publicly Traded Companies

As far as is known, there are no disclosure or other obligations on shareholders in publicly traded companies.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Pursuant to Article 137 of the AUSCGIE, at the close of each fiscal year the manager or the board of directors or the general manager (as the case may be) must prepare and close the financial statements in accordance with the provisions of the Uniform Act on the Organisation and Harmonisation of Companies' Accounting.

As required by the revised Article 140 of the AUSCGIE, for an SA, an SAS and (where applicable) a SARL, the annual summary financial statements and the management report are sent to the auditors at least 45 days before the date of the ordinary general meeting. These documents are presented to the general meeting of the company approving the financial statements, which must be held within six months of the end of the financial year.

6.2 Disclosure of Corporate Governance Arrangements

Pursuant to Article 138 of the AUSCGIE, the manager, the board of directors or the general manager (as the case may be) draws up a management report in which they describe the situation of the company during the past financial year, its foreseeable evolution, the important events that occurred between the closing date of the financial year and the date on which it is drawn up, and – in particular – the prospects for the continuation of the activity, the evolution of the cash-flow situation and the financing plan.

This report is therefore financial, but the AUSCGIE, allows for the creation of committees – composed of directors, within the board and under the direction of a director – to deal with particular aspects of the life of the company

(Article 437 of the AUSCGIE). Thus, according to Article 437 Section 2 “[The board of directors] may decide to create committees composed of directors to study the questions that it or its chair[person] submits to them for advice. It shall determine the composition and powers of the committees, which shall carry out their activities under its responsibility.”

The AUSCGIE, also provides for the mandatory presence of audit committees in companies issuing stock to the public, in order to ensure better corporate governance. The audit committee must report regularly to the board of directors on the performance of its duties and must inform the board of directors without delay of any difficulties encountered (Article 829-1 of the AUSCGIE).

In addition, agreements entered into directly or through an intermediary between the company and one of its managers, directors or shareholders are the subject of a special report by the auditor at the general meeting.

6.3 Companies Registry Filings

In Côte d'Ivoire, companies are created through the *Centre pour la Promotion de l'Investissement en Côte d'Ivoire* (CEPICI). This organisation acts as a link between the various administrations, creating a unique identification number required by all administrations.

Commercial companies are required to make filings with the companies registry of the registered office for the following:

- the appointment or termination of the functions of company executives (Article 124 of the AUSCGIE);
- a draft merger or demerger (filed in the Trade and Personal Property Credit Register of the

registered office of the companies concerned at least one month before the date of the first general meeting called to decide on the operation) (Article 194 of the AUSCGIE);

- the dissolution of the company, by filing in the Trade and Personal Property Credit Register the deeds or minutes deciding upon or recording the dissolution and by amending the entry in the Trade and Personal Property Credit Register (Article 202 of the AUSCGIE);
- liquidation of the company by the deposit of the final accounts drawn up by the liquidator, with either the decision of the meeting of shareholders ruling on these liquidation accounts, the discharge of the liquidator's management and the discharge of their mandate, or – failing this – the court decision referred to in the preceding article in order to obtain the striking-off of the company from the Trade and Personal Property Credit Register (Articles 219 and 220 of the AUSCGIE);
- approval of the company's accounts by filing the summary financial statements (ie, the balance sheet, the profit-and-loss account, the financial table of resources and uses, and the annexed statement of the past financial year) within one month of their approval by the competent body (Article 269 of the AUSCGIE);
- transferable securities (for their enforceability against third parties); and
- transfer of shares (for the enforcement of their rights against third parties) (Articles 319 and 763-1 of the AUSCGIE).

The filings relating to the incorporation or the modification of the company (merger, liquidation of a company) as well as the pledges or the collective procedure are publicly available upon request to the companies registry. However, specific documents such as financial statements are not available. Failure to make these filings

entails the unenforceability of the modifications/actions carried out.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

In the SA, the appointment of an auditor is mandatory. It takes place during the constitutive general meeting (for the first appointment). An SA making a public appeal for savings is required to appoint at least two auditors and two deputies. An SA that does not make a public offering is required to appoint one auditor and one substitute.

As regards the other corporate forms, this appointment is optional, except where the company exceeds certain thresholds (see **1.1 Forms of Corporate/Business Organisations**).

The auditor's duties include:

- evaluating the contributions in kind realised at the time of the constitution of a SARL or an SA;
- drafting the summary financial statements;
- presenting the agreements between the company and its shareholders or its directors to the general meeting or the board of directors; and
- making requests to the company's directors concerning all facts likely to compromise the continuity of the operation, which they have noted during the examination of the documents that are communicated to them, or of which they have knowledge in the exercise of their duties.

The auditor is responsible, with respect to the company and third parties, for the harmful consequences of the faults and negligence they may

commit in the performance of their duties (insufficient investigation or certification of an inaccurate balance sheet, for example).

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Management Report (Article 138 of the AUSCGIE)

The manager, the board of directors, or the general manager (as the case may be) is required to prepare a management report in which they describe the situation of the company during the past financial year, as well as its future situation. This management report is submitted to the approval of the shareholders at the annual general meeting.

Agreements Between the Company's Directors and the Company

In an SA with a board of directors (Article 438 of the AUSCGIE) and an SA with a general manager (Article 502 of the AUSCGIE), the regulated agreements are subject to the authorisation of the members of the board of directors and to the approval of the general meeting ruling on the summary financial statements. For a SARL (Article 350 of the AUSCGIE) and an SAS (Article 853-14 of the AUSCGIE), these agreements are subject to approval by the general meeting.

Prohibited Agreements

The managers of a SARL (Article 356 of the AUSCGIE) and the directors of an SA (Article 450 of the AUSCGIE) are prohibited from contracting loans from the company in any form whatsoever, from being granted an overdraft on a current account or otherwise, as well as from being guaranteed or endorsed by the company in respect of their commitments to third parties. These acts are null and void.

Trends and Developments

Contributed by:

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Houda Law Firm is a multi-sectoral and multi-disciplinary law firm based in Senegal and Côte d'Ivoire. The firm has a total staff of 53 people, comprising a team of lawyers, jurists and paralegals. The staff work in French and English to ensure the satisfaction of local and international clients. Houda Law Firm provides legal advice and assistance to a diverse clientele in

a variety of practice areas, including business law, insurance law, banking and finance, public and private international law, contract law, mining, oil and gas, renewable energy, and tax. The firm has proven expertise in the energy and extractive sector, as well as in PPPs, banking and finance, and corporate and commercial law.

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The Beneficial Ownership Register: An Effective Tool for Combating Money Laundering in the OHADA Region?

The transparency of corporate structures has become a major issue in the African economic landscape, increasingly marked by a strong desire to attract foreign investment. At the same time, money laundering is emerging as a major challenge for the economies of the Organisation for the Harmonisation of Business Law in Africa (*Organisation pour l'Harmonisation en Afrique du Droit des Affaires*, or OHADA) member states.

Indeed, in a context where illicit financial flows – estimated at between USD50 and USD90 billion dollars per year, according to the United Nations – deprive Africa of vital resources, African states have gradually strengthened their AML frameworks. The introduction of transparency mechanisms, such as the beneficial ownership register, constitutes a direct response to these challenges.

This article aims to analyse the scope and effectiveness of this register within the OHADA region by examining its legal framework, modalities of implementation, sanction regimes, and perspectives for future development.

Definition and legal framework

The obligation to maintain a beneficial ownership register represents a true innovation under Ivorian law, as well as in several other OHADA member states, since such a requirement did not previously exist in the OHADA Uniform Acts themselves.

In Côte d'Ivoire, Article 49 ter (new) of the Tax Procedure Code provides: “Commercial companies and civil companies, regardless of their form and activities, must keep at the disposal of the Administration a register of their beneficial

owners. The beneficial owner is defined in paragraph 11 of Article 1 of Law No 2016-992 of 14 November 2016, relating to combating money laundering and the financing of terrorism. The register referred to above must be kept up to date with any changes affecting the beneficial ownership of the legal entity and presented upon any requisition by the Administration.”

Thus, the beneficial owner, also known as the economic beneficiary, is defined as:

- the natural person(s) who ultimately own(s) or control(s) a client; and/or
- the natural person on whose behalf a transaction is conducted.

This definition also includes those who ultimately exercise effective control over a legal entity or legal arrangement.

The threshold commonly applied aligns with international standards, meaning a direct or indirect ownership of at least 25% of the share capital or voting rights. However, control may also be exercised through other means, such as specific statutory provisions or shareholder agreements.

The primary objective of the register is to enhance financial transaction transparency by preventing legal entities from concealing the true identity of the individuals behind them.

The establishment of the beneficial ownership register in the OHADA region comes in an increasingly demanding international context, driven by organisations such as the World Bank and the Financial Action Task Force (FATF), of which several OHADA member states are members.

Furthermore, Directive No 02/2015/CM/UEMOA of 2 July 2015, concerning anti-money laundering and counter-terrorism financing, incorporates provisions requiring the identification of beneficial owners.

In Côte d'Ivoire, Law No 2024-362 of 11 June 2024, establishing the beneficial ownership register for legal entities and legal arrangements, has further reinforced this framework.

Implementation of the register in OHADA member states

The aforementioned external influences - notably, the recommendations of FATF - have led to the progressive emergence of a legal framework adapted to the region's specificities while meeting international standards, which aims at strengthening transparency in legal structures across the OHADA region.

At the community level, the Uniform Act on Commercial Companies and Economic Interest Groups (*Acte Uniforme révisé relatif au droit des Sociétés Commerciales et du Groupement d'Intérêt Économique*, or AUSCGIE) now imposes - through Articles 744-1, 746-1 and 746-2 - an obligation for each covered entity to maintain an internal register of its beneficial owners. However, the AUSCGIE, does not yet mandate the creation of a centralised register accessible to the authorities or to the public. Therefore, the concrete organisation and publicity of the registers depend on the domestic laws of each OHADA member state.

The transposition of the obligation to maintain a beneficial ownership register reveals notable disparities among OHADA member states. Some countries, such as Côte d'Ivoire, Senegal, Cameroon, and Benin, have adopted specific legislation that even goes beyond the minimum

requirements of the AUSCGIE. Other states are still in the process of adopting implementing texts or operationalising the mechanism.

Depending on the country, three main models for implementing the register can be observed:

- direct integration into the RCCM (*Registre du Commerce et du Crédit Mobilier*) - in some countries (such as Côte d'Ivoire), information relating to beneficial owners is incorporated into the registration or modification procedures recorded at the RCCM, which acts as the public reference registry;
- creation of a distinct register - other states have set up a separate register (although it is still recorded and certified by the RCCM); and
- management of the register by specific AML authorities.

Practical modalities for maintaining the beneficial ownership register

Within the OHADA region, the following entities are required to declare their beneficial owners:

- commercial companies governed by the AUSCGIE, (*société à responsabilité limitée* (SARL), *société anonyme* (SA), *société par actions simplifiée* (SAS), *société en nom collectif* (SNC), etc);
- civil companies, when subject to registration with the RCCM;
- branches of foreign companies operating within a member state; and
- economic interest groups (EIGs).

The information generally required under the national laws of OHADA member states is aligned with international standards. Each entity must collect and record in its internal register the following:

- the full identity of the beneficial owner (name, surname, date of birth and place of birth);
- their personal address;
- the nature (direct or indirect ownership) and extent of the interests held (precise percentage of ownership); and
- the modalities of the control exercised over the entity.

The regular updating of this information is mandatory, particularly in the event of a change of beneficial owner or a substantial modification of their situation.

Sanctions regime and effectiveness in case of non-compliance with declaratory obligations

Sanctions applicable for failure to declare beneficial owners - whether administrative and financial, civil and commercial, or criminal - are structured on two regulatory levels, as follows.

- At the community level, the AUSCGle, does not specifically provide for sanctions directly linked to beneficial owners, but it establishes a general framework for offences related to declaratory obligations.
- At the national level, the legislation transposing AML instruments defines more specific sanctions.

Administrative and financial sanctions vary depending on the member states but generally include administrative fines, which in Côte d'Ivoire range from XOF100,000 to XOF1 million (approximately EUR150 to EUR1,500) (cf Article 11 of Law No 2024-362 of 11 June 2024, mentioned previously), as well as daily penalties in case of continued non-compliance (generally between XOF50,000 and XOF200,000 per day of delay).

These sanctions are generally imposed by tax authorities responsible for verifying the existence and maintenance of the register or by the national AML authority.

Failure to declare or the submission of false information may also lead to:

- civil liability of company directors towards the company or third parties harmed by the default; and
- judicial dissolution of the company in cases of repeated and deliberate violations.

In most OHADA member states, criminal sanctions are also provided for:

- the deliberate submission of inaccurate or misleading information about beneficial owners (punishable by imprisonment from six months to three years, depending on the country);
- obstruction of inspections conducted by competent authorities (punishable by imprisonment from one month to one year); and
- complicity in concealing the true identity of beneficial owners (sanctions aligned with those applicable to money laundering).

Despite the existence of this repressive framework, several factors influence the effective enforcement of sanctions within the OHADA region:

- a relatively recent implementation in most member states, with an initial focus on raising awareness before entering a repressive phase;
- limited and fragmented understanding by authorities of the risks associated with legal entities, despite the frequent use of corpo-

- rate structures to conceal money laundering activities;
- significant disparities in the capacity for control and supervision between different member states;
- limited case law and the absence of reliable databases specifically relating to infractions linked to the beneficial ownership register;
- insufficient information exchange mechanisms between national authorities to detect cross-border violations;
- limited accessibility and reliability of essential information, given that informal economic activities remain significant in the region - resources available to the RCCM do not allow for thorough verification to ensure the accuracy and update of declared information;
- the General Directorate of Taxes (*Direction Générale des Impôts*, or DGI) provides, upon request and in a timely manner, information on beneficial owners kept in the registers of legal entities - however, regular and sufficient audits of the registers maintained by the entities themselves are lacking; and
- the RCCM does not have the authority to sanction individuals or legal entities that fail to provide or update basic information about a legal entity - although tax authorities have reportedly imposed occasional sanctions on non-compliant legal entities, the effectiveness, proportionality, and dissuasiveness of such sanctions have yet to be firmly established.

Impact of the register on AML efforts in the OHADA region

Despite its recent introduction and gradual implementation, the beneficial ownership register is beginning to have positive effects on economic practices within the OHADA region. Some stakeholders are increasingly reconsidering the use of complex corporate structures, and pro-

fessionals such as notaries, business lawyers, and accountants are progressively integrating beneficial ownership obligations into their advisory services.

For financial intelligence units and judicial authorities across the OHADA region, the beneficial ownership register constitutes an essential complementary tool in investigations, given that:

- it facilitates the identification of links between various legal structures involved in suspicious operations;
- it allows for the detection of discrepancies between financial flows and declared beneficial owners; and
- it provides a useful documentary basis for international co-operation in combating financial crime.

However, its preventive impact remains limited, owing to:

- partial awareness of the system among economic operators (particularly among SMEs and within the informal sector); and
- uneven application of the sanctions foreseen for failure to comply with declaratory obligations.

Thus, while the beneficial ownership register already represents real progress in strengthening financial transparency and fighting illicit financial flows, its full potential has yet to be realised. Effective enforcement mechanisms, better information-sharing practices, and increased awareness among private sector stakeholders remain crucial to ensuring the register's success.

Future prospects and recommendations

To strengthen the implementation and effectiveness of the beneficial ownership identification

system within the OHADA region, several legal developments could be considered, as follows.

- Adoption of a specific Uniform Act - a dedicated Uniform Act focused on AML, including detailed provisions on beneficial ownership, would strengthen the consistency of the system at the community level.
- Clarification of identification criteria - a clearer definition of the criteria for identifying beneficial owners, adapted to the African economic and cultural context, would facilitate the proper application of the system.
- Strengthening sanctions - harmonising and reinforcing sanctions for incomplete or erroneous declarations would contribute to the system's effectiveness.

Beyond the legal framework, several technical improvements could also enhance the effectiveness of the register, as follows.

- Deepening the understanding of the topic - strengthening awareness among authorities and reporting entities about the risks associated with legal persons must be a priority.
- Interconnection of national registers - setting up an interconnection between the registers of different OHADA member states (potentially through the Regional File established by the 2018 Regulation) would enable more effective action against cross-border arrangements.
- Development of automated verification tools - integrating tools capable of automatically detecting inconsistencies in declarations would improve the reliability of collected information.
- Raising awareness among economic operators - targeted information campaigns would enhance understanding and acceptance of the system by businesses.

- Support for professionals (lawyers, notaries, accountants) - developing practical guides and offering specific training would help these professionals better advise their clients regarding their declaratory obligations.

In conclusion, it should be noted that the beneficial ownership register represents a significant step forward for financial transparency and the fight against money laundering in Africa. Its gradual deployment within the OHADA region - albeit still uneven among member states - responds to an increasing international demand for transparency and accountability of legal entities.

The sanction regime associated with this system - characterised by its multi-layered nature and evolving structure - plays a crucial role in ensuring the effectiveness of the declaratory obligation. However, the heterogeneity of national approaches and the challenges related to the concrete application of sanctions remain points of attention.

To maximise the register's impact, it will be necessary to address specific challenges inherent to the OHADA context:

- limited administrative capacities;
- co-ordination across multiple regional frameworks; and
- adaptation to local socio-economic realities.

Moving towards a stronger harmonisation of sanctions at the community level and integrating appropriate technological innovations appear to be promising avenues for strengthening this essential pillar of Africa's financial integrity.

From this perspective, enhanced cooperation between the various stakeholders - the OHADA Permanent Secretariat, national courts, financial

intelligence units, professional bodies - appears critical to success. Ultimately, the effectiveness of the beneficial ownership register as a tool for preventing and repressing money laundering within the OHADA region will depend on the collective ability to mobilise all concerned actors.

In summary, if fully implemented and modernised, the beneficial ownership register could become a strategic tool to ensure legal security, foster investment, and effectively combat illicit financial flows within the OHADA region.

ETHIOPIA

Law and Practice

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TBeST Law LLP



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TBeST Law LLP is a full-service law firm that provides corporate and commercial legal services across a wide range of sectors and practice areas. It draws on over 50 years of the collective experience of its partners in the academic and legal services sectors. As one of the leading firms in the country, the firm's lawyers are at the forefront of Ethiopia's legal reform, contributing to the drafting of the Ethiopian

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Eight different forms of business organisations are recognised under the Ethiopian Commercial Code of 2021:

- sole proprietorship;
- general partnership (GP);
- limited partnership (LP);
- joint venture (JV);
- limited liability partnership (LLP);
- private limited company (PLC);
- one-person company (OPC); and
- share company (SC).

Foreign businesses can also operate business via “*branches*” or “*commercial representative offices*” (CROs). Foreign companies that win international competitive bids operate in Ethiopia by opening “*Project Offices*” or “*Contract Offices*”.

The primary vehicles for doing business with limited liability are the private limited company (PLC) and share company (SC).

A share company is an entity that is closest to a public company, formed by either founders or public subscription.

A private limited company is established usually by family or closely-related persons, but it is also a preferred form of business for foreign companies seeking to establish subsidiaries in Ethiopia. A private limited company may be used to undertake most types of businesses except financial services of banking and insurance, for which a share company is a requirement. The shares of private limited companies are not open for public subscription.

A one-person private limited company (OPC) is the newest form of business organisation introduced by the new Commercial Code of Ethiopia. The OPC is incorporated by one person and operates like a private limited company. Although the OPC operates similarly to a limited liability company, the member of a one-person private limited company, or any other person who directly or indirectly controls the company, is jointly and severally liable with the company if found to have committed any of the following acts:

- intentionally commits an unlawful act that jeopardises the interests of the company or its creditors;
- intermingles the assets of the company with their personal assets;
- fails to maintain a clear distinction between their personal identity and that of the company;
- deliberately provides misleading financial information about the company's status to its creditors;
- utilises the company's assets for personal gain or the benefit of third parties without appropriate compensation to the company;
- receives dividends exceeding the legally permitted maximum; or
- commits other similar acts.

1.2 Sources of Corporate Governance Requirements

The main legislative source for corporate governance is the Commercial Code of Ethiopia, issued in 2021 (Proclamation No 1243/2021). Additional and special corporate governance requirements are also provided for in the Commercial Registration and Licensing Proclamation No 980/2016 (as amended by Proclamation No 1150/2019) and regulations and directives issued thereunder.

Special corporate governance requirements for banks and insurance companies are provided under sector-specific laws. For banks, these requirements are now primarily governed by Banking Business Proclamation No 1360/2025, which repealed the earlier Proclamation No 592/2002 (as amended by Proclamation No 1159/2019). This new proclamation marks a major shift, as it opens Ethiopia's previously closed banking sector to foreign investment, allowing foreign banks to operate in the country

for the first time. This is a landmark move in the broader financial sector liberalisation agenda.

For insurance companies, corporate governance requirements are set out in the Insurance Business Proclamation No 746/2013, as amended by Proclamation No 1163/2019, and the relevant directives and regulations issued thereunder.

With the advent of capital markets in Ethiopia, corporate governance requirements concerning publicly listed companies are in the works. However, ECMA has issued key directives, including the Capital Market Service Providers Licensing and Supervision Directive No 980/2024, which sets out corporate governance standards for capital market service providers.

In addition to the laws mentioned above, companies provide for additional corporate governance requirements in their memorandums of associations and by-laws.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

The Ethiopian Capital Market Authority (ECMA) was established by Proclamation No 1248/2021 as the sector's regulator.

The Capital Markets Proclamation No 1248/2021 contemplates that notices and guidelines on corporate governance will be issued for publicly listed companies. A Directive on corporate governance for publicly listed companies, as a result, appears to be under development. Nevertheless, ECMA has issued the Public Offer and Trading of Securities Directive No 1030/2024, effective from 13 November 2024, which governs public offerings and trading. ECMA has also required all publicly held companies to disclose detailed information on their share structures.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In recent years, corporate governance in Ethiopia has been influenced by a range of factors including economic reforms, international business practices, and changes in the legal and regulatory environment. The following are some hot topics in corporate governance in Ethiopia.

Corporate Governance Frameworks and Best Practices

Efforts to develop and implement corporate governance frameworks and codes of conduct that align with international best practices are ongoing. This is particularly the case for State Enterprises. This includes strengthening transparency, accountability, and ethical conduct within corporations.

Transparency and Disclosure

Enhancing transparency in financial reporting and corporate disclosures is a key focus. This includes ensuring timely and accurate financial statements, as well as clear communication with shareholders and other stakeholders.

Minority Shareholder Rights

Strengthening the rights of shareholders, particularly minority shareholders, and encouraging greater engagement in corporate decision-making are important topics particularly after the passing of the New Commercial Code.

Digital Transformation and Cybersecurity

With the rise of digital transformation, companies are focusing on cybersecurity and data protection to safeguard against cyber threats and data breaches. The newly passed Data Protection Proclamation No 1321/2024 will also contribute significantly to the handling and storage of data by companies.

Privatisation and Foreign Investment

As Ethiopia continues to open up its economy to foreign investment and privatisation, there is an increased emphasis on establishing robust corporate governance standards to attract and retain investors.

Legislative Reform

With a number of legislative changes taking place, companies are working overtime to ensure they are up to date and compliant with laws that have been passed. Ethiopia has seen extensive legislative reform in the past years including a revision of the Commercial Code, investment laws, and the passing of new legislation such as the Data Protection Proclamation. The country has also opened up a number of sectors, including banking, telecoms and other parts of trading sectors.

In addition to the above, the Council of Ministers has introduced a draft proclamation that seeks to regulate the ownership and use of immovable property by foreign nationals in Ethiopia. This development represents a potential turning point in the country's long-standing legal framework governing land and property ownership which prohibited foreigners from owning immovable property including land, as well as residential and commercial buildings, in Ethiopia – except in special circumstances provided under investment laws.

The draft proclamation has been submitted to the House of People's Representatives (HoPR) for review and potential enactment. If adopted by Parliament, the proposed legislation would signal a major policy shift, potentially opening new avenues for foreign investment in the real estate and broader corporate sectors. This legislative reform may affect corporate governance by necessitating more robust compliance and

transparency mechanisms to manage increased foreign ownership and ensure alignment with local regulatory standards.

2.2 ESG Considerations

Companies and their directors are encouraged to take into consideration the environmental and social implications of their project. In this regard, Ethiopia has enacted a new proclamation on environmental impact assessment, Proclamation No 1371/2025, which states that an environmental social impact assessment certificate will be essential for projects which will be categorised by directives to be enacted under the proclamation. Pursuant to the repealed Environmental Impact Assessment Proclamation No 299/2002, specific sectors, particularly manufacturing, energy, and mining, were required to submit environmental impact assessment plans as a fundamental condition for obtaining business licenses. Waste management plans remain a prerequisite for obtaining business licenses in the manufacturing, energy, and mining sectors.

A new introduction under the new Environmental Impact Assessment Proclamation is the requirement for a social impact assessment. The Proclamation defines Social Impact as *“the negative or positive impact of a development plan on peoples’ lifestyles, relationships and community organization”*. The Environmental Impact Assessment Certificate (EIAC) that will be issued by the Environmental Protection Authority also encompasses permits for social impact assessment. Investment projects cannot be implemented without obtaining the EIAC. This development may compel companies to integrate broader environmental and social responsibility measures into their strategic decision making and risk management frameworks.

With regards to corporate governance, the by-laws of business organisations must contain standard corporate governance rules that are provided for in the Commercial Code. The law commits the parties to higher standards of corporate governance.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

One-Member Company

A one-member private limited company is a company formed through the membership of only one person or entity. The one member has the mandate to exercise the powers of the general meeting of shareholders of a private company.

Limited Company

The rules governing a private limited company shall apply as appropriate to a one-member private limited company.

Private Limited Company and Share Company

Private limited companies and share companies are governed and managed by specific bodies or functions as defined under the Ethiopian Commercial Code.

General Meeting of Shareholders

The general meeting of shareholders is the highest decision-making body. It consists of all the shareholders of the company and holds meetings at least annually.

Board of Directors

The board of directors is responsible for the overall governance and strategic direction of the company. The board is elected by the share-

holders and oversees the company's operations. It makes decisions on behalf of the company, appoints the general manager (if applicable), and ensures that the company complies with laws and regulations. The board also has the authority to establish committees (eg, audit committee) to assist in its governance responsibilities. A private limited company may have a board of directors if provided for in its memorandum of association. The board of directors of a private limited company may consist of between three and seven members, while the board of a share company has between three and 13 members. Ethiopian law permits non-shareholders to be board directors, but the number of non-shareholder directors should not exceed one-third of the number of directors.

General Manager

Both private limited companies and share companies have a general manager appointed by the general meeting or the board of directors, if one exists. The general manager may be a shareholder or an outsider, and shall not be the chairperson of the board. Additionally, the general manager is an employee of the company and is responsible for the day-to-day management of the company. The general manager shall be liable to the company, shareholders and third parties for any damage caused by breach of their duties under the law or the memorandum of association of the company. In bankruptcy and where the assets of the company are found to be inadequate, the general manager may be liable to settle the company's debts or part of them along with the previous managers of the company.

Supervisory Board

A share company may have a supervisory board where its memorandum of association provides the same. The supervisory board is composed

of three to five members who can only be shareholders of the company. The members of the supervisory board are appointed by and are accountable to the general meeting of shareholders. The general meeting of shareholders shall also determine the remuneration of the members of the supervisory board. Additionally, members of the supervisory board are not permitted to be members of the management of the company or members of the board of directors. The meeting time for the supervisory board shall be determined by the memorandum of association of the company.

Secretary

A share company shall have a secretary who is appointed by the board of directors upon the recommendation of the general manager. The secretary is accountable to the general manager.

External Auditors

All share companies are required to have an independent and impartial external auditor and assistant auditors, which are appointed by the general meeting of shareholders. A shareholder representing at least 20% may appoint an auditor. The general meeting of the shareholders decides on the remuneration of the auditor. Ethiopian law additionally permits both individuals and corporate entities to act as auditors of a share company. Auditors are appointed for up to three-year terms.

Private limited companies will be required to have an external auditor if they have ten or more members or if the total assets of the company exceed ETB10 million. The auditor in a private limited company will also be appointed by the general meeting of the shareholders.

3.2 Decisions Made by Particular Bodies

The various management bodies have different mandates. Please see 3.1 Bodies or Functions Involved in Governance and Management for details on the mandates of the shareholders' meetings.

Shareholders' Meetings

The general meeting of shareholders holds two types of meeting: ordinary and extraordinary shareholders' meetings.

Ordinary general meeting of shareholders

A meeting will be called by the board of directors, by the manager where there is no board or it fails to call the meeting, or in case of failure by the preceding by the auditor, if any, or by members representing more than one-half of the capital of the company.

A meeting is to be held once at least within four months from the end of the financial year. The four-month period may be extended for up to six months.

An ordinary general meeting can expect to see the following on the agenda:

- amend, approve or reject, after discussion, the balance sheet, the profit and loss account as well as reports of the board of directors, reports of the auditors and supervisory board, if any, and where necessary, pass resolutions relating to the allocation of and distribution of profits and on all questions arising out of the accounts for the past financial year;
- appoint or remove directors, members of the supervisory board or auditors as appropriate and decide the amount of their remuneration;
- approve the issue of debentures as well as the guarantees attached thereto;

- approve transfer of 51% or more of the assets of the company at once or within one year from the date of the first sale at different intervals; and
- decide all matters on which a general meeting passes decisions other than those specifically reserved to an extraordinary general meeting.

Extraordinary general meeting of shareholders

This meeting has the authority to make major decisions such as amending the memorandum of association, increasing or reducing the capital of the company, appointing a liquidator, deciding on dissolution, conversion, division or merger of the company, and changing the nationality of the company.

Board of Directors

- Quorum – majority of directors must be present unless a greater vote is required by the memorandum of association.
- Decision-making – majority of directors who are present personally, by proxy and by electronic means. Unless provided otherwise, the chairperson shall have a casting vote in case of a tie.
- Mandates – the directors have a duty to perform the tasks imposed on them by law, the memorandum of association and resolutions of the general meeting of shareholders. In particular they shall:
 - manage the company's finances with a view to ensuring that the company has adequate capital and liquidity to meet its liabilities in a timely manner;
 - ensure that the company's governance arrangements are such as to ensure the proper monitoring of the company's financial statements and positions;

- make certain that sufficient procedures for risk management and internal control are established;
- provide to the supervisory board, if any, all information needed for the performance of the duties of the supervisory board in a timely manner; and
- prevent damage to the company, or where prevention is not possible, mitigate adverse impact of acts which are prejudicial to the company.

Without prejudice to what is stated above, the directors shall be responsible for:

- keeping regular records of the meetings of the board of directors and shareholders, accounts and books, registers of shareholders and directors and other necessary documents;
- ensuring submission of accounts and books to auditors when required;
- submitting an annual report of the company's operations including a financial statement to the general meetings of shareholders;
- convening meetings as provided in Commercial Code or memorandum of association;
- convening an extraordinary general meeting without delay where three-quarters of the capital of the company is lost;
- setting up the reserve funds required by law or memorandum of association or resolution of general meeting of shareholders; and
- where the company's ability to meet its financial obligations diminishes or where it suspends payment of debt applying, as appropriate, for preventive restructuring, reorganisation or bankruptcy.

Supervisory board – the supervisory board of a share company may have the following powers and duties in addition to those that may be

assigned to it by the memorandum of association of the company:

- causing the submission of documents and information necessary to discharge its responsibility, and examine the same;
- calling and leading a general meeting of shareholders, where the board of directors is unable or unwilling to convene such a meeting;
- taking part and giving opinion in the meeting of the board of directors without voting.
- where it comes to know or has reason to suspect that an act that causes damage to the company has been committed, investigating the matter or cause it to be investigated or, take the necessary measures with the view to instituting legal action, if need be;
- undertaking supervision to ensure that directors and other members of the management are discharging their responsibilities properly;
- where it has been ascertained that they have committed an act that jeopardises the interests of the company, demanding that corrective measures be taken;
- recommending the removal of those who have failed to discharge their responsibilities properly, as appropriate, to the board of directors or general meeting of shareholders;
- supervising as well as causing the auditing of the financial affairs of the company;
- submitting reports to the general meeting; and
- carrying out other functions as may be assigned to it by the memorandum of association or resolution of the general meeting of shareholders.

General Manager

The general manager is responsible for the day-to-day management of the company.

Unless expressly provided in the by-laws, the general manager represents the company in its dealings with third parties. In addition, the general manager has the power to:

- sign and transfer negotiable instruments, especially commercial instruments, transferable securities and documents of title to goods;
- discharge responsibilities entrusted to them by the memorandum of association;
- discharge responsibilities entrusted to them by the board of directors and implement its decisions;
- prepare an annual work plan and budget of the company and implement the same upon approval by the board of directors; and
- hire, manage and fire the employees of the company, as necessary.

Secretary

The role of the secretary is to:

- organise and keep information and records of the company;
- provide reports and other necessary information promptly to a concerned body;
- provide information to shareholders and third parties;
- organise meetings of shareholders and members of the board of directors;
- prepare, organise and keep minutes; and
- carry out other tasks assigned to it by the general manager and memorandum of association.

Auditor

The auditor in both a private limited company and share company has significant responsibility. Some of these duties include:

- discharge their duties following generally accepted accounting principles;
- provide accurate information;
- treat shareholders equally;
- keep professional secrets;
- keep the duty to inform of irregularities;
- annually verify the correctness and accuracy of the inventories, balance sheets, and profit and loss accounts, books and other financial documents;
- certify that the report submitted by the board of directors to the general meeting of shareholders reflects the correct state of the company;
- provide written comment on the report of the board of directors to the general meeting of shareholders, recommend to the general meeting to approve or reject the accounts submitted by the directors and comment on the proposal for distribution of profits submitted by the directors;
- call general meetings where the directors or supervisory board fails to call a meeting required by law or the memorandum of association;
- call general meetings where shareholders representing at least 10% of the capital so requests; and
- carry out such other duties as may be assigned to them in the memorandum of association or by a general meeting of shareholders.

3.3 Decision-Making Processes

Please see **3.2 Decisions Made by Particular Bodies** and **5.3 Shareholder Meetings** for the decision-making process for these bodies.

4. Directors and Officers

4.1 Board Structure

The board of directors in a private limited company is composed of between three and seven members, while the board of a share company is composed of between three and 13 directors. The members of the board are elected by the shareholders. The board members may be either shareholders or non-shareholders. The law provides that two-thirds of the members of the board may not play a role in the day-to-day management of the company. Additionally, the law provides that non-member directors may not exceed one third of the total membership of the board.

The board may elect a chairperson or a deputy chairperson among its members. The law provides that it is only a member who is a shareholder that may be appointed as a chairperson.

The board is also permitted to grant any one or more of its members a special mandate, including the mandate to represent the company in a specific transaction.

4.2 Roles of Board Members

The general meeting of the shareholders or the memorandum of association may provide details as to the mandate of the chairperson, as well as board committees. The Commercial Code, however, provides only for the roles of the chairperson or the directors in general. Please see 3.2 **Decisions Made by Particular Bodies** for details of the duties of the directors.

4.3 Board Composition Requirements/Recommendations

Board members are required to meet the following criteria to qualify as such:

- minimum age specified by the memorandum of association or law, if any;
- being of good moral character;
- no record of conviction of breach of trust, theft, robbery or other similar criminal offences while serving as a promoter, director, manager, member of supervisory board or auditor or holding any other managerial position or under any other circumstance; and
- compliance with other requirements set by the memorandum of association or another law, if any.

Where there are different classes of shares in a company, each class of share is required to appoint at least one representative a member of the board.

4.4 Appointment and Removal of Directors/Officers

Members of the board of directors may be appointed for the first time by the memorandum of association and subsequently the general meeting of shareholders. Directors may be removed at any time by the general meeting of the shareholders. It is important to note that a director who is removed without good cause cannot be reinstated but can only claim damages for the wrongful dismissal.

4.5 Rules/Requirements Concerning Independence of Directors

As indicated below, one of the legal duties of directors is the legal duty to exercise independent judgement and avoid conflict of interest. Ethiopian law restricts directors from partnering or taking part either directly or indirectly in a rival business or competing with the company. Directors are also required to avoid situations that may lead to a conflict of interest with the company. This includes the exploitation of the company's property, information or opportunity

of the company regardless of whether the company used the same.

Directors have a duty to disclose any situation as soon as the existence of the situation is known that may be or lead to a conflict of interest. The director shall disclose the nature and extent of that interest to the other directors. A director is also prohibited from receiving a gift or any other type of benefit from a third party for being a director. Given the clear conflict of interest, directors are restricted from voting on matters like a proposed agreement between the director and the company or any other person where the director may derive an essential benefit from the transaction.

4.6 Legal Duties of Directors/Officers

Directors and officers of a company have the following legal obligations under Ethiopian law.

- Duty of care and diligence – directors are required to discharge their duties with care, skill and diligence and may be liable for failure to do so.
- Duty to exercise independent judgement.
- Duty of loyalty – directors must act in a way that promotes the success of the company and benefit all shareholders.
- Restriction on private trade – unless expressly permitted by the general meeting, directors are restricted from partnering in rival business or competing against the company directly or indirectly.
- Duty to avoid conflict of interest – directors must avoid situations that have or may have direct or indirect conflict of interest with the company.

4.7 Responsibility/Accountability of Directors

Directors are accountable to the general meeting of shareholders. They are at all times required to act in good faith and loyalty to the best interest of the company and for the benefit of the shareholders as a whole.

4.8 Consequences and Enforcement of Breach of Directors' Duties

The company may enforce a breach of the duties of the directors of the company only with a resolution of the general meeting of shareholders. If the company fails to implement such a resolution within three months, shareholders representing 10% of the capital may jointly institute proceedings in the name of the company. Additionally, shareholders who have sustained damages from a personal injury directly owing to the fault or fraud of a director may bring legal action directly.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Under Ethiopian law, any agreement protecting the directors from liability is of no effect regardless of its form – ie, in the memorandum of association or a contract with the company. The company may, however, maintain an indemnity insurance to protect board members from liability. Additionally, the company may maintain a special fund for the legal defence of its directors against actions by administrative bodies, creditors or shareholders subject to refund if the directors lose the case.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The general meeting of shareholders is required to fix and approve the annual remuneration of directors in a lump sum. The ordinary general meeting of the company may grant directors

specified share in the net profit of a financial year which shall in no case exceed 10% of the net profit that may be distributed as dividend for the fiscal year.

For companies like banks and insurance companies, the National Bank of Ethiopia has strict caps for the disclosure requirement as well as a cap on the amount and type of remuneration directors may receive. Currently, the cap on annual compensation to be paid to board directors of banks and insurance companies is ETB150,000, and the maximum monthly allowance is ETB10,000, both to be paid upon the decision of the ordinary general meeting of the shareholders.

Additionally, any public companies listed on an exchange are required to disclose a list of their directors, remuneration, salaries and incentives as reported to the general meeting of shareholders. Failure to comply with these disclosure requirements for financial institutions and listed companies may lead to a fine being imposed on the company.

4.11 Disclosure of Payments to Directors/Officers

Please see 4.10 Approvals and Restrictions Concerning Payments to Directors/Officers. Additionally, every share company is required to keep a register of its directors and officers including details on their address, directorship, and responsibility in any other businesses. This register is open to shareholders and government authorities who are permitted to examine it free of charge. Non-shareholders may also examine this register for a fee.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The relationship between a company and its shareholders in Ethiopia is primarily defined by the company's memorandum of association and the Ethiopian Commercial Code. Shareholders are the owners of the company through shares that are to be registered in their names. The obligations of shareholders are limited to making the contribution they pledged to make to the company. On the other hand, shareholders have certain rights, such as:

- voting at shareholders' meetings;
- receiving dividends and proceeds on winding-up;
- preferred right for subscription of new shares; and
- the right to information about the company's affairs.

The rules and requirements governing this relationship include the Ethiopian Commercial Code, securities regulations, and commercial registration and licensing requirements. Companies are often required to provide regular financial reports to shareholders, hold annual general meetings, and ensure transparency and fairness in their dealings with shareholders. Additionally, there are specific rules regarding the rights of minority shareholders and the responsibilities of company directors and officers such as the general manager and auditors.

5.2 Role of Shareholders in Company Management

Shareholders play a crucial role in the management of a company under the Ethiopian Commercial Code, although their involvement is limited to certain key decisions. One important

aspect is that only a shareholder director can become the chairperson of the board of directors. Additionally, the number of non-shareholder directors is restricted not to exceed one-third of the total membership of the board of directors.

Furthermore, shareholders representing at least 20% of the capital of the company can appoint an auditor selected by them. This gives them a significant say in the financial oversight of the company. A general meeting of shareholders can also resolve to institute proceedings against its directors, even if it is not on the agenda. If the company fails to institute proceedings within three months, shareholders representing at least 10% of the capital have the right to institute proceedings in the name of the company. This demonstrates their ability to hold the management accountable for their actions.

In terms of decision-making, general meetings of shareholders have the authority to amend, approve, or reject the balance sheet, the profit and loss account, reports of the board of directors, reports of the auditors and supervisory board, if any. They can also pass resolutions relating to the allocation and distribution of profits and make decisions on various matters such as appointing or removing directors, members of the supervisory board or auditors, and deciding the amount of their remuneration.

Moreover, it is shareholders that have the power to amend the memorandum of association of the company, increase or reduce the capital, change the nationality of the company, and decide on dissolution, conversion, division, or merger of the company.

5.3 Shareholder Meetings

The Ethiopian Commercial Code mandatorily requires the holding of an ordinary general

meeting of shareholders within four months from the end of each financial year with a possibility of extension to six months under the by-laws of a company. The Commercial Code outlines specific rules and requirements for ordinary general meetings (OGM) and extraordinary general meetings (EGM) to govern the conduct of such meetings. EGMs can be convened whenever necessary.

Mode and Time of Calling Meetings

In terms of convening shareholder meetings, the responsibility falls on various entities, including the directors, supervisory board, auditors, liquidators, or even the court in exceptional cases. Additionally, the Ministry of Trade and Regional Integration or a similar entity may also call for meetings under specific circumstances. Shareholders are notified of these meetings through registered letters, emails, or other reliable electronic methods, with the company bearing the expenses associated with the notification process.

The timing of the notice is critical, with a minimum of 24 days required for the first OGM or EGM. In cases where a quorum is not met, subsequent meetings can be called. For an OGM, the same 24 days is given for a second meeting while there is no specific date for subsequent meetings called for lack of quorum. For an EGM, second and third meetings can be called at one-week intervals. The content of the notice is mandated to include essential details such as the company's name, capital, head office, meeting specifics, and the agenda to be discussed during the meeting.

Quorum

Quorum requirements vary for OGMs and EGMs. For OGMs, at least 1/4th of voting shares is required for the first meeting, while the second

meeting can proceed irrespective of the number of voting shares represented. In contrast, EGMs have more stringent quorum requirements, with at least half of voting shares needed for the first meeting, 1/3rd for the second meeting, and 1/10th for the third meeting.

Majority

The majority required for passing resolutions also differs between OGMs and EGMs. OGM decisions are taken by a simple majority, disregarding abstentions, and blank ballots. In comparison, EGMs require at least a 2/3rd majority for a resolution to be adopted, with specific agenda items, such as changing the nationality of the company, requiring unanimity.

5.4 Shareholder Claims

Under the Ethiopian Commercial Code, shareholders have various avenues for claims against the company or directors. Shareholders become creditors of the company for dividends due to them from the date fixed for payment. In addition, the provisions of the Code outline the legal duties of directors and describe potential violations that may result in liabilities for the company. These include:

- requirements for good moral character and compliance with the memorandum of association;
- obtaining necessary approvals and disclosures in related-party transactions;
- approval and independent auditor reports for fund transfers involving directors;
- ensuring adequacy of capital, liquidity, and proper governance arrangements;
- consistently acting in the best interests of shareholders and the company's long-term sustainability; and
- avoiding personal interest entanglement with company affairs, and ensuring requisite care,

skill, and diligence in managing the company's affairs, among others.

The Commercial Code also specifies the procedures for enforcing the liability of directors, including the necessity of a resolution of a general meeting of shareholders to institute proceedings against directors. If the company fails to institute proceedings within three months, shareholders representing at least 10% of the capital have the right to institute proceedings in the name of the company. Shareholders also have the right to bring legal action for damages if they have been directly injured by the fault or fraud of the directors.

Claims for damages against directors and members of the supervisory board are subject to a limitation period of two years from the date when the aggrieved party knew of the damage and the perpetrator, with an absolute limitation after ten years from the date when the act in question occurred.

5.5 Disclosure by Shareholders in Publicly Traded Companies

There are disclosure obligations on shareholders in publicly traded companies as provided under the Ethiopian Capital Market Proclamation. According to the applicable legal provisions, an *"Interested Person"* is defined as any person who has an interest representing 5% or more in the capital of a company listed on an exchange, whether directly, indirectly, or in alliance with others.

Such Interested Persons are required to submit an authenticated and signed statement to the Capital Markets Authority (the *"Authority"*), the Exchange where the securities are traded, and to the issuer of those securities within five days of acquiring the interest. According to the Pub-

lic Offering and Trading of Securities Directive No 1030/2024 (the “*Directive*”), the name of any person, other than a member of the Board of Directors who, directly or indirectly, has an interest in the issuer’s capital or voting rights of 5% and above should be revealed, together with the amount of each such person’s interest, as of the date of the prospectus. If there are no such persons, an appropriate statement that attests that no such person exists should be submitted to the Authority. Other information that needs to be disclosed as per the Directive are the following:

- (a) whether the issuer’s major shareholders have different voting rights, or an appropriate statement to the effect that no such voting rights exist;
- (b) whether there is an agreement in place to govern the relationship between a controlling shareholder, another interested persons and the issuer; and,
- (c) a description of any arrangements known to the issuer, the operation of which may, at a subsequent day, result in a change in control of the issuer.

Additionally, any share company listed on an exchange is required to disclose the names of interested persons and any changes in their shareholding. The exchange is also required to announce the information received concerning the disclosures of interests immediately upon receipt.

Failure to disclose the interest as described above, and Directives to be issued by the Authority, may result in liability for any damages incurred by the Authority, the exchange, or a third party.

Furthermore, interested persons and share companies listed on an exchange are required

to report to the Authority and the Exchange any changes in interest that exceed more than 0.5% of the issuer’s capital within ten days of the date of the change. This reporting remains mandatory until the change results in a decline of the interest to below 5% of the capital.

Additionally, share companies listed on an exchange are required to maintain a special register for the disclosure of the members of the board of directors, executive directors, and managers, which involves all statements and information determined by the Authority. This register is also required to include all data related to remunerations, salaries, incentives, and other financial benefits as included in the report of the General Assembly, and stakeholders have the right to access this register during regular working hours.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Companies must adhere to a set of financial reporting obligations as stipulated in the Ethiopian Commercial Code on an annual and periodic basis. These obligations encompass the compilation of:

- a comprehensive inventory of the company’s assets;
- a balance sheet;
- a profit and loss statement; and
- a report on the company’s activities and affairs over the previous financial year.

Additionally, company directors are required to submit these documents to auditors, the Ministry of Trade and Regional Integration, or other relevant government authorities at least 40 days

prior to dispatching notices for the annual general meeting.

Furthermore, it is mandated that the balance sheet and profit and loss statement be prepared annually in the same format as in prior years, unless variations are approved by the general meeting upon the recommendation of the auditors.

For a holding company, the accounts of its subsidiaries must be presented at the annual general meeting simultaneously and in the same manner as its own accounts, alongside the preparation of a consolidated balance sheet and profit and loss statement.

In circumstances where the board of directors deems it impractical or burdensome to prepare such documents, or if it may be detrimental to the company or its subsidiaries, they have the option to seek exemption from these obligations, subject to approval by the Ministry of Trade and Regional Integration or other relevant government authority.

In addition, any self-regulatory organisation participating in capital markets is required to submit audited financial statements to the Capital Markets Authority within four months after the end of every financial year. The Authority is yet to issue Directives providing the specifics of the audited financial statements that must be disclosed by issuers of public offerings and listed companies.

6.2 Disclosure of Corporate Governance Arrangements

Under the Ethiopian Commercial Code, the board of directors is responsible to ensure that the company's governance arrangements are such as to ensure the proper monitoring of the company's financial statements and positions.

Moreover, directors have the obligation of submitting an annual report of the company's operations including a report on the company's activities and affairs over the previous financial year to the general meetings of shareholders, auditors and the Ministry of Trade and Regional Integration. These responsibilities show the obligation to disclose the corporate governance arrangements in the reports. However, there are no specific corporate governance codes that are required to be adhered to in these reports.

In addition, any self-regulatory organisation participating in capital markets is required to submit a report on its corporate governance policy and practices along with its annual report to be submitted to the Capital Markets Authority within four months after the end of every financial year.

6.3 Companies Registry Filings

In Ethiopia, it is the Ministry of Trade and Regional Integration that establishes and administers a Federal Commercial Register, having a nationwide application. Companies are required to make several filings with this Ministry, including:

- the submission of the inventory, balance sheet, profit and loss account, and directors' report;
- detailed information on related-party transactions involving conflicts of interest;
- details regarding a more than 5% reciprocal holding of shares between two companies;
- details by non-wholly-owned subsidiaries on whether their management is directed by the parent company;
- notification of change of business address;
- notification of any alternation or amendment on commercial registration such as company name, general manager, capital, additional business, etc;

- the balance sheet, along with the relevant part of the minute of approval by the meeting; and
- any changes in the particulars of the share register which contains particulars of members, transfers of shares, and any amendments to these particulars.

The Commercial Code and the Commercial Registration and Licensing Proclamation (as amended) both provide that the commercial register and trade name register must be open and accessible to the public at large. Third parties are entitled to look into the register or demand from the appropriate registering office the issuance of a copy of any extract from the register or, where an entry has not been made into the register, a certificate to the effect that no such entry has been made.

In addition, members have the right to consult the share register kept by companies free of charge, and any third party may do so upon payment of a prescribed fee. If inaccuracies are found in the register, the Ministry of Trade and Regional Integration or relevant government authority may cause rectification, and the company's directors or managers are liable for any losses resulting from such inaccuracies.

Failure to make these filings and comply with the disclosure requirements results in legal consequences. For instance, failure to notify changes of business address and other changes warranting amendment of the commercial register are punishable with fine and imprisonment. This is in addition to the potential liability for any losses due to inaccuracies in filings or failure to disclose the required information.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

All share companies are required to have independent and impartial external auditors and assistant auditors that are appointed by the general meeting of shareholders. All private limited companies with members of more than ten, or private limited companies with total assets exceeding ETB10 million are also required to have independent and impartial external auditors appointed by the general meeting of shareholders.

Auditors appointed as external auditors must possess professional licence from the Auditing and Accounting Board of Ethiopia, and must be of good moral character. Auditors may not be a shareholder or an employee of the company, and many not in any event be affiliated with the company as directors, managers, or secretaries. Auditors have the duty to discharge their duties following generally accepted accounting principles, provide accurate information, treat shareholders equally, keep professional secrets, annually verify the correctness and accuracy of financial statements and certify that the report submitted by the board of directors reflects the correct state of the company. Auditors also have the duty to compile complete information on conflicts of interest and submit information together with their recommendations to the general meeting of shareholders.

For more detail on the powers and duties of the auditor, please see **3.2 Decisions Made by Particular Bodies**.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Directors have the duty to make certain that sufficient procedures for risk management and internal control are established. In particular, directors have the responsibility of ensuring that the company has adequate capital and liquidity to meet its liabilities in a timely manner, ensure that the company's governance arrangements are such as to ensure the proper monitoring of the company's financial statements and positions, ensure submission of accounts and books to auditors when required, set up the reserve funds required by the law; and where the company's ability to meet its financial obligations diminishes or where the company ceases making payments, apply for preventive restructuring, reorganisation or bankruptcy, as appropriate.

FRANCE



Law and Practice

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Aurès

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Aurès is a specialist corporate and dispute resolution firm, combining expert legal advice with the focus and flexibility of a boutique practice. Building up its extensive experience, the team routinely assists companies, boards of directors, investors and senior executives in high-stakes corporate transactions (M&A, tender offers, squeeze-out, spin-offs, joint ventures) and corporate governance matters (CEO suc-

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1. Introductory

1.1 Forms of Corporate/Business Organisations

In France, most business organisations are incorporated in the form of companies with distinct legal personality.

French law distinguishes between civil companies, governed by civil laws exclusively, and commercial companies, governed by civil and commercial laws. Civil companies may operate only a limited list of activities, which are deemed civil by nature (eg, agriculture, liberal activities, real estate), while commercial companies may operate any type of activities, including civil activities.

There are three main differences between civil companies and commercial companies:

- civil companies may not conduct commercial or industrial activities – their purpose is therefore limited;
- shareholders' liability is never limited in civil companies, whereas it is limited in most commercial companies; and
- most civil companies are tax-transparent – ie, profits of the company are taxed at the shareholders' level and subject to income tax, whereas most commercial companies are subject to corporate tax.

These differences explain that civil companies are far less common than commercial companies, and limited to specific uses. For this reason, they will be excluded from this study.

The corporate forms applicable to commercial companies are numerous and can be classified into two categories: limited liability companies and unlimited liability companies. Unlimited lia-

bility companies are rare and used for extremely specific transactions, so they will be also excluded from this study.

Among limited liability companies, the most common corporate forms are:

- public limited companies (*sociétés anonymes* or SA), used for large companies, most listed companies being incorporated in the form of SA;
- simplified joint stock companies (*sociétés par actions simplifiées* or SAS), a rather new corporate form but largely used thanks to its high flexibility; and
- limited liability partnership (*sociétés à responsabilité limitée* or SARL), primarily used for small businesses, as shares of SARL are not freely tradable.

1.2 Sources of Corporate Governance Requirements

Corporate governance requirements are derived from laws and regulations, recommendations and internal rules set forth by companies themselves.

Laws and Regulations

The French Commercial Code (*Code de commerce*) and, to a lesser extent, the French Monetary and Financial Code (*Code monétaire et financier*) contain the majority of corporate governance rules and requirements.

European Union directives and regulations, such as the Shareholder Rights Directive II of 17 May 2017, or the Directive on improving the gender balance among directors of listed companies dated 23 November 2022, also comprise a set of corporate governance requirements applicable to French companies. Requirements issued from EU directives shall be incorporated into French

law in order to be enforceable, whereas requirements issued from EU regulations are directly applicable to French companies.

Recommendations

Listed companies are subject to additional recommendations issued by corporate governance codes to which they must refer (or explain why they decided not to), such as the AFEF-MEDEF Code, intended for large, listed companies, and the Middledenext Code, intended for small and medium-sized listed companies.

They must also take into consideration recommendations issued by the *Haut Comité au Gouvernement d'Entreprise* (HCGE) – a special committee appointed to follow the implementation of the AFEF-MEDEF Code and interpret its recommendations – the French Financial Markets Authority (AMF) and the *Haut Comité Juridique de la Place financière de Paris* (HCJP).

To a lesser extent, listed companies may also take into account the voting policies issued by proxy advisers (Proxinvest, ISS), as they are followed by a majority of investors and give a guidance on satisfactory governance policies for investors.

Internal Rules

Finally, companies may adopt internal rules, such as by-laws, board internal regulations, codes of ethics or of conduct, which set forth specific corporate governance rules and requirements.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Listed companies are subject to additional mandatory corporate governance requirements and recommendations.

First of all, only three corporate forms are authorised to trade their shares on a regulated market: SA, *Societas Europaea* (SE) and partnerships limited by shares (*société en commandite par actions* or SCA).

Listed companies are subject to other mandatory corporate governance requirements.

- Composition of the board of directors (*conseil d'administration*) – the composition of listed companies' boards of directors (or supervisory boards) is highly regulated. Listed companies are subject to gender balance requirements (the proportion of directors of each gender must be at least 40%) and requirements related to the appointment of directors representing employees and employee shareholders (please refer to **4.3 Board Composition Requirements/Recommendations**).
- Audit committee – listed companies are required to set up an audit committee whose purpose is to provide technical and critical support to management in monitoring the company's accounting and financial policy (please refer to **4.1 Board Structure**).
- Compensation of corporate officers ("say-on-pay") – listed companies must comply with the "say-on-pay" requirements for the determination and payment of corporate officers' and directors' compensation. The "say-on-pay" proceedings require a double shareholders' approval on compensations: the shareholders shall vote on the compensation policy determined by the board of directors (ex-ante vote) and on the amounts payable to corporate officers and directors upon implementation of the approved compensation policy (ex-post vote).
- Enhanced governance information – listed companies must include, in their management reports, additional corporate govern-

ance and ESG information as well as all relevant information on factors that are likely to have an impact in the event of a tender offer. Listed companies must also publish relevant information regarding related-party agreements.

Listed companies are also subject to various recommendations, including:

- appointment of independent directors – (please refer to **4.5 Rules/Requirements Concerning Independence of Directors**);
- set up of specialised committees – (please refer to **4.1 Board Structure**); and
- limitation of allowances – listed companies shall be prudent with allowances granted to directors and/or officers and subject these allowances to performance criteria and limit their overall amount.

Recommendations applicable to listed companies mostly derive from corporate governance codes. Although these codes are deemed to be non-binding (soft law), listed companies choosing not to follow their recommendations must publicly explain why and justify their choice to the market (comply-or-explain principle). In addition, companies choosing not to follow recommendations issued by the AMF may be named in the AMF corporate governance report for not complying with its recommendation.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance Green Shareholder Activism and “Say-on-Climate”

Shareholder activism is increasingly focusing on ESG and climate-related issues. Since 2020, activist investors have started to request issuers

operating in high-impact sectors (energy, building industry) to consult their shareholders on their climate strategy, on the say-on-pay model. If most motions proposals submitted in 2020 and 2021 were rejected by the board of directors or disapproved at the general meeting, issuers took into account this new issue and included related consultative resolutions at the 2023 general meetings. In this context, the HCJP published a report in December 2022, and the AMF a press release in March 2023, encouraging listed companies to submit “say-on-climate” resolutions for shareholders’ approval every year. A proposal to introduce “say-on-climate” statutory regime including new obligations for listed companies with a view to improve their climate strategy was made as part of the discussions on the Green Industry Act in 2023, but was in the end rejected by the French legislature.

Expansion of Multiple Voting Rights Shares

French corporate law has long abandoned the rule “1 share = 1 vote” by allowing the issuance of shares with multiple voting rights. However, their use was still restricted for listed companies until the *Attractivité* Act of June 2024. Before, listed companies could only issue shares with double voting rights to long-term shareholders: other forms of multiple voting rights were prohibited.

In line with the EU Listing Act, the French legislature has allowed the issuance of multiple voting rights through preferred shares during the initial public offering of a company on a French regulated market or multilateral trading facility. This law has established mandatory safeguards – which may be supplemented by the by-laws – such as:

- limitation of the voting ratio to 25:1 for shares listed on a multilateral trading facility – no

- such restriction applies to shares listed on regulated markets;
- neutralisation of multiple voting rights for certain resolutions, such as approval of the annual accounts, appointment of the auditors, amendments to the by-laws not related to share capital increases, approval of related-party agreements, and say-on-pay; and
- conversion of the preferred shares into ordinary shares in the event of an insolvency proceeding of the company, a transfer of ownership or after ten years (which may be extended by a maximum of five years), resulting in the loss of multiple voting rights, except if the ordinary shares resulting from such conversion meet the standard conditions for double voting rights (ie, fully paid-up, registered shares held by the same shareholder for at least two years), it being specified that the period during which the preferred shares were held in registered form prior to conversion is taken into account.

Transposition of the Directive “Women on Boards”

Article 5 of the “DDADUE” Act published in the *Journal Officiel* of 23 April 2024, empowers the government to transpose the “Women on boards” Directive (EU Directive of 23 November 2022, on a better gender balance among directors of listed companies). For the record, under the Copé-Zimmerman Act of 27 January 2011, the board of directors must be composed of at least 40% of each gender. The transposition Ordinance of 15 October 2024 includes, in the calculation basis for the gender diversity obligation, the employee shareholder representatives and the employee representatives sitting on these boards for all companies, whether listed or not, with at least 250 employees and either a turnover or a balance sheet total exceeding EUR50 million. This will enter into force on

30 June 2026 for companies falling under the “Women on Boards” Directive and on 1 January 2027 for others.

Progressive Entry Into Force of the Rixain Act

Since March 2022, companies with at least 1,000 employees for three consecutive fiscal years have been required to publish data on gender inequalities among executive managers and governing bodies. By March 2026, these companies must ensure at least 30% representation of each gender among executive managers and governing bodies, increasing to 40% by March 2029. A two-year grace period will be granted for compliance, after which financial penalties may apply.

Extra-Financial Reporting and CSRD Directive

Please refer to 2.2 ESG Considerations.

Network and Information Security 2 (NIS 2) Directive

The NIS 2 Directive is a strengthened version of the NIS 1 Directive, the first version of which was designed to control data protection for companies operating in so-called “essential” sectors (such as energy, water, health and transport) in the face of the cyber threat. Despite the obligation to transpose the NIS 2 Directive by 17 October 2024, many European countries – including France where the text was adopted by the *Sénat* in March 2025 and transmitted to the *Assemblée Nationale* – are still in the process of implementation.

The NIS 2 Directive imposes two major governance obligations: make management bodies responsible for managing risks to networks and IT systems and implement a training policy on security issues for members of management and staff.

In other words, management bodies will need to be increasingly involved in cyber risk management. They will also be held accountable if they fail to meet their obligations.

2.2 ESG Considerations

ESG and Strategy

The board of directors is entrusted with the definition of the strategy of the company. In doing so, the board is legally bound to take into account social and environmental issues.

Year after year, corporate governance codes increase their recommendations towards a better consideration of climate and environment protection-related issues, with the recommendations to create an ESG committee, in charge of investigating ESG matters or the enhanced training of directors or the increase of ESG performance criteria as part of executives' compensation schemes.

Also, pressure to increase climate strategy reporting to shareholders is in constant evolution (please refer to 2.1 Hot Topics in Corporate Governance).

Corporate Duty of Care

Since 2017, the largest French companies have been subject to due diligence obligations to identify any risks and prevent any violations of human rights and fundamental freedoms, or severe abuses of human health and safety and of the environment, resulting from their activities as well as those of their subsidiaries, suppliers and subcontractors. These companies must establish a vigilance plan and a report on its effective implementation, to be included in the annual report.

The European Union has recently adopted the Corporate Sustainability Due Diligence Directive

(CSDDD), published on 5 July 2024, providing for similar due diligence obligations applicable to EU limited liability companies of substantial size and economic power or with business in defined high-impact sectors. Following the adoption of the “*Stop the Clock*” Directive in April 2025, the transposition deadline for the CSDDD has been postponed. The CSDDD will now enter into force in two phases, with the first wave starting on 26 July 2028 for the largest companies, and the second on 26 July 2029 for a broader range of businesses, including certain non-EU companies.

Raison d'être and Mission-Driven Companies

In 2019, the Pacte Act introduced two optional tools into French corporate law designed for companies intending to redirect their focus on their role in society, beyond their economic performance: the concept of *raison d'être* (core purpose), as well as the status of mission-driven company.

The *raison d'être* determines the orientation of a company's business and defines its identity and vocation, beyond its commercial purpose. Therefore, a company adopting a *raison d'être* makes the choice to define the ethical standards according to which its activities will be conducted. Companies adopting a *raison d'être* are free to define it more or less precisely. One can observe that there is a great deal of variation in the level of precision and relevance of the chosen *raison d'être*, which has an impact on the effectiveness of this tool in terms of creating new ethical standards: the more generic the *raison d'être*, the less likely it is to clarify the standards binding the company.

The Pacte Act also allows French companies complying with stricter requirements to be labelled as mission-driven companies. This sta-

tus may be granted to companies choosing to adopt – in addition to a *raison d'être* – strong commitments towards environmental, ethical and/or social concerns. These commitments are submitted to the general meeting of shareholders and included in the by-laws. Compliance with these commitments is assessed regularly by a mission committee, comprising at least one employee and usually representatives of other stakeholders. Failure to comply with the mission or the commitments not only entails the withdrawal of the status, but could also lead to liability claims against the directors and the company.

Extra-Financial Reporting and CSRD Directive

French listed companies and other large companies are subject to extra-financial reporting obligations in the form of a non-financial performance declaration (DPEF). These requirements will be drastically extended starting in 2024 with the entry into force of the Corporate Sustainability Reporting Directive (CSRD) of 14 December 2022, transposed within French law by the Ordinance dated 6 December 2023. CSRD provides for the substitution of a new extended reporting on sustainability, in order to include information on environmental, social and governance issues. The reporting requirements will be based on a double materiality principle: sustainability matters that affect the company as well as the impacts of the company on sustainability matters.

Information contained in this new sustainability report (to be included in the annual management report) will be certified by authorised auditors or independent third-party organisations. In addition, shareholders holding at least 5% of the capital or voting rights may request the appointment of another auditor or independent third-

party organisation to draft a separate report on part of, or all sustainability information.

Following the adoption of the “*Stop the Clock*” Directive in April 2025, the timetable for the application of the CSRD has been adjusted. Large listed companies with more than 500 employees, already subject to the CSRD, must report on the 2025 financial year, with reports published in 2026. Other large companies and parent companies of large groups, not covered by the first wave, will be required to report on the 2027 financial year, with publication in 2028. Listed small and medium-sized enterprises, excluding micro-enterprises, will be required to report on the 2028 financial year, with publication in 2029. In order to guide companies, the ESMA, the European Commission, and the *Haute Autorité de l'Audit* have respectively published recommendations, Q&A and guidelines.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

There are three main functions involved in the governance and management of French companies:

- deliberative functions;
- supervisory functions; and
- management functions.

Deliberative Functions

Deliberative functions are always delegated to the shareholders of the company. Depending on the corporate form, shareholders' decisions are mandatorily adopted in general meetings (eg, SA) or may result, if the company's by-laws allow it, from their unanimous consent expressed in a written act (eg, SAS, SARL).

Supervisory Functions

In elaborate forms of companies, specific bodies are responsible for supervising management, whereas in other forms of companies, management control is left to the shareholders.

In SA with a one-tier board system, the board of directors is a hybrid corporate body as it is in charge of supervisory functions over corporate officers, as well as certain management functions (please see below). Most supervisory functions are assigned to the supervisory board.

In other corporate forms (SAS, SARL), supervisory functions are performed, in a more limited way, directly by the shareholders and no dedicated corporate body is provided by law. However, the shareholders may decide, in SAS, to create specific corporate bodies and entrust them with supervisory powers.

Management Functions

Management functions include the definition and implementation of the company's strategy and the representation of the company towards third parties. Depending on the corporate form of the company, management functions are exercised by individuals or collegiate bodies.

SA may be structured pursuant to a one-tier board or a two-tier board system, at the shareholders' discretion. This choice must be registered in the by-laws.

In SA with a one-tier board system, the management functions are split between the board of directors, whose members are appointed by the shareholders, the chairman of the board of directors, appointed by the board among the directors, and the CEO (*directeur général*), also appointed by the board of directors. The board of directors may also decide to name a single

person to act as chairman and CEO (*président-directeur général*). The board of directors, upon request of the CEO, may appoint one or more deputy CEOs to assist the CEO and delegate management powers to them.

In SA with a two-tier board system, the management functions are entrusted to the executive board (*directoire*), appointed by the supervisory board. Members of the executive board are not allowed to be part of the supervisory board.

In SAS, the law entrusts the chairman (*président*) with all management functions. The chairman may be a natural or a legal person. The shareholders are free to provide for additional corporate bodies in the by-laws, entrusted with limited management functions.

SARL are managed by one or more managing directors (*gérants*). The managing directors are natural persons.

3.2 Decisions Made by Particular Bodies

The powers and types of decisions made by the corporate bodies differ depending on the corporate form of the company.

Please refer to **5.2 Role of Shareholders in Company Management** for a description of the shareholders' decision-making powers.

SA

In one-tier board systems, the board of directors is competent to determine the strategic orientations of the company's business and ensure their implementation within the limits of the company's interest and taking into consideration social and environmental issues. In particular, the board of directors:

- appoints the chairman and the CEO and defines their compensation schemes;
- examines and approves the annual financial statements;
- drafts management reports for the shareholders;
- convenes the general meeting of shareholders and sets forth its agenda; and
- approves related-party agreements.

The powers of the board of directors shall be exercised within the limits of the corporate scope of the company and the power granted by law to the general meeting of shareholders.

The CEO, and the deputy CEOs, if any, are in charge of the day-to-day management of the company, within the limits of the corporate object of the company and the board of directors' and the general meeting's powers. Vis-à-vis third parties, the CEO has the broadest powers to represent the company and act on its behalf, even those exceeding the corporate scope and the limitations of powers that may result from the by-laws. However, those limits may only be enforced towards third parties if it is proven that they had knowledge of such limitations.

In two-tier board systems, the supervisory board is responsible for the supervision of the management and the preservation of the company's long-term interest. Therefore, the supervisory board:

- appoints the members of the management board and defines their compensation schemes;
- controls the annual financial statements;
- reviews the management reports; and
- approves related-party agreements.

Unlike the board of directors, the supervisory board is not entitled to make management decisions.

The executive board is in charge of the strategy of the company and its day-to-day management, within the limits of the general meeting's powers. The chairman of the executive board has broadest powers to represent the company towards third parties.

SAS

The chairman of the SAS is the only mandatory management body of the company, and is therefore entrusted with the broadest powers to manage the company within the limits of the shareholders' powers and represent it towards third parties.

The shareholders may set other corporate bodies to assist or supervise the chairman. Internally, the chairman's powers shall be limited by specific powers granted to these corporate bodies. The shareholders may also decide to limit the chairman's powers in the by-laws and require prior authorisation from the shareholders for material decisions. Those limits may, however, be enforced towards third parties only if it is proven that they had knowledge of such limitations.

SARL

In the SARL, each of the managing directors has the broadest powers to manage the company within the limits of the corporate scope and shareholders' powers. The same rules regarding third parties apply to the managing directors.

The role and powers of the shareholders are described in **5.2 Role of Shareholders in Company Management**.

3.3 Decision-Making Processes

The applicable decision-making process depends on the nature of the corporate body. Please refer to **5.3 Shareholder Meetings** for the shareholders' decision-making processes.

Collegiate management and/or supervisory bodies meet periodically on a pre-defined agenda. Meetings are called by the chairman and the convening process is freely determined in the by-laws or other internal rules, if any. For the adoption of defined decisions, such as the approval of annual or interim accounts, the statutory auditors (if any) must be given notice of the meeting. In companies with at least 50 employees, members of the social and economic committee (*comité social et économique*) may also attend the meetings in an advisory capacity.

In SA, the board of directors may also implement specialised committees whose role is to issue opinions on matters submitted by the board and falling into their competence area. In this case, the board of directors will be convened after the relevant committee and will make decisions based on the committee's opinion.

Decisions are made by a vote of the general meeting, which may be held physically, via videoconference, or by postal vote. In this regard, the majority and quorum rules are defined by law or the internal documentation of the company. By exception, and if so provided for in the by-laws, decisions may result from the unanimous consent of the shareholders, expressed in a written act. Decisions are registered in minutes – drafted by an external secretary or by a member of the corporate body – executed by the chairman of the meeting and usually at least one other member of the body.

Recent reforms introduced by the *Attractivité* Act and its implementing decree have further modernised corporate governance practices by facilitating remote decision-making.

Subject to by-law authorisation, shareholder meetings (excluding those of listed companies and the annual ordinary shareholder meeting convened to approve the financial statements in SARL) and board meetings may now be held entirely via telecommunication. In any case, shareholders of SA and SCA may attend, by such means, physically held meetings. By-laws may also allow written consultation – which may be conducted electronically – and postal voting for shareholders and board decisions (provided no board member objects). New requirements also apply to the transmission, recording and consultation of general meetings for listed companies as further detailed in **5.3 Shareholder Meetings – Extraordinary General Meetings**.

French law does not dictate any decision-making process for non-collegiate corporate bodies, although it is recommended that material management decisions are registered in writing. In addition, the by-laws or other internal rules may enforce voluntary decision-making process.

4. Directors and Officers

4.1 Board Structure

SA

As mentioned in **3.1 Bodies or Functions Involved in Governance and Management**, SA may be structured pursuant to a one-tier board or a two-tier board system.

Given the relative scarcity of the two-tier board system, **4.1 Board Structure** to **4.11 Disclosure**

of Payments to Directors/Officers will only deal with one-tier board SA.

SA boards of directors are composed between three and eighteen directors, including the chairman of the board. The shareholders appoint the directors, which may be natural or legal persons. In the latter case, they must appoint a permanent representative to the board.

Regulations and recommendations apply to the selection of directors:

- diversity rules require boards of directors of companies having more than 250 employees to have a proportion of directors representing each gender at the board of at least 40%;
- larger companies must appoint directors representing the employees or shareholders' employees; and
- corporate governance codes recommend that a sizable proportion of directors are independent.

The board of directors may set up specialised committees (audit committee, compensation committee, ESG committee, etc), whose role is to issue opinions on matters submitted by the board in order to improve the effectiveness of the board. Specialised committees have consultative powers only and are not a substitute for the board. Audit committees are mandatory for companies whose shares are admitted to trading on a regulated market.

The shareholders may also appoint censors to the board of directors, with an advisory role only.

SAS

In SAS, the structure of the board – if the shareholders decided to voluntarily set up such col-

legiate body – is freely set in the by-laws or internal rules adopted by the shareholders, if any.

SARL

There is no board of directors in SARL, as the management is exclusively performed by its manager(s).

4.2 Roles of Board Members

The board of directors is a collegiate body. As a principle, the directors collectively exercise the functions assigned to the board and they do not have any individual powers, except for the chairman of the board.

However, the board of directors may grant specific assignments to individual directors, in order to improve the corporate governance of the company and facilitate the board's mission.

Directors may be assigned, given their skills and experience, to one or more specialised committees to help assess specific matters (please refer to 4.1 Board Structure).

Also, the board of directors may appoint a lead director chosen from among the independent directors to play a mediating role between the board of directors and the shareholders and improve shareholder dialogue. Lead directors are strongly recommended by the AFEP-MEDEF Code in a controlled listed company.

The chairman of the board has a distinct role: they are in charge of organising and directing the work of the board of directors and reporting to the general meeting. The chairman ensures the proper functioning of the company's bodies and that the directors are able to fulfil their duties.

4.3 Board Composition Requirements/Recommendations

Various regulations and recommendations apply to the selection of directors and the composition of the board.

- Number of directors – the board of directors shall be composed of at least three and at most 18 directors, including the chairman. Within these limits, the number of directors is determined by the by-laws.
- Natural or legal person – directors may be natural or legal persons, except for the chairman who must be a natural person.
- Share ownership – it is not mandatory for directors to hold shares of the company, but the by-laws may provide otherwise.
- Diversity – boards of directors of companies having more than 250 employees shall comprise a proportion of directors representing each gender at the board of at least 40%, or, if the board is composed of eight or less directors, the difference between the representatives of each gender shall not exceed two.
- Age limit – in accordance with the French Commercial Code, not more than a third of the directors may be aged over 70, but the by-laws may provide for a stricter age limit.
- Multiple directorships – directors may not hold more than five directorships in public limited companies, it being understood that directorships in affiliated companies are excluded for the calculation of the directorships.
- Representation of employees – in large companies, employees are entitled to appoint directors representing the employees to the board of directors.
- Representation of employee shareholders – in large companies where more than 3% of the share capital is held by employees, the share-

holders shall appoint directors representing the employee shareholders.

- Independence – corporate governance codes recommend that, in listed companies, a sizable proportion of directors should be independent (please refer to **4.5 Rules/Requirements Concerning Independence of Directors**).

4.4 Appointment and Removal of Directors/Officers SA

Directors are appointed and may be dismissed at any time, without cause (*ad nutum*) by the general meeting of shareholders. Given that the agenda of the general meeting is set by the board of directors, shareholders are allowed to vote on the appointment and dismissal of one or more directors even if these decisions were not registered in the agenda. When a seat at the board of directors becomes vacant, the board is entitled to provisionally appoint a new director to fill the vacancy, subject to ratification by the next general meeting.

The chairman of the board, whether they assume the CEO position or not, is appointed by and among the directors of the board and must be a natural person. The chairman may be dismissed at any time, without cause by the board of directors. If the chairman is dismissed from their role as director by the shareholders, the chairman is automatically dismissed from the chairman and, as the case may be, CEO position.

If the chairman does not assume the CEO's position, the CEO is appointed by the board of directors. Deputy CEOs may also be appointed by the board of directors upon proposal from the CEO. The CEO and deputy CEOs must be natural persons. The CEO and deputy CEOs may be dismissed at any time by the board of

directors. The CEO and deputy CEOs may however claim damages if dismissed without cause (*juste motif*).

The appointment of directors must also comply with the aforementioned legal requirements (please refer to **4.3 Board Composition Requirements/Recommendations**).

SAS

The chairman is appointed and dismissed in accordance with the by-laws or internal rules of the company. In case the by-laws do not provide any details regarding the conditions of dismissal, the chairman may be dismissed at any time, without cause.

SARL

The managing directors of the SARL are appointed and dismissed by the general meeting of shareholders at any time but, in the absence of cause, may claim damages.

4.5 Rules/Requirements Concerning Independence of Directors

There are no requirements concerning the independence of directors in non-listed companies.

With respect to companies whose securities are admitted to trading on a regulated market, the French Commercial Code indirectly requires the appointment of independent directors, since the audit committee must include at least one director deemed independent according to criteria specified and made public by the board of directors.

Also, the corporate governance codes recommend that a sizeable proportion of directors be independent. Hence, the AFEF-MEDEF Code recommends that 50% of directors be inde-

pendent in not-controlled companies, and 33% in controlled companies.

The corporate governance codes set up a list of criteria for the assessment of the independence of directors. The board of directors shall use those criteria to determine which directors are independent, it being understood that even if all criteria are not met, the board remains free to deem a director independent if it is otherwise justified.

4.6 Legal Duties of Directors/Officers

Corporate officers and directors must act in accordance with the best corporate interest of the company, with the additional requirement provided by the Pacte Act enacted in 2019 to “take into consideration” social and environmental issues when making their decisions.

The scope of directors’ duties expanded with the publication of the Corporate Sustainability Due Diligence Directive on 5 July 2024, requiring companies to mitigate their negative impact on human rights and the environment, including at the procurement, production and distribution levels, even though France has already had a similar framework since 2017.

4.7 Responsibility/Accountability of Directors

Directors and officers must act in accordance with the best interest of the company, which generally overlaps with that of the shareholders, but it is not systematic. In this respect, directors and the board are becoming increasingly pivotal in the implementation of new ethics standards in corporate strategy, with new or renewed interests to be taken into consideration (employees, other stakeholders, etc) when assessing the situation vis-à-vis the corporate interest of the company they manage.

4.8 Consequences and Enforcement of Breach of Directors' Duties

According to the circumstances, a breach of directors' or officers' duties may be enforced by the following parties:

- the company, by an *ut universi* action brought through its legal representative. The action can also be brought by a shareholder when the company is held liable for breaches committed by its legal representative. In such case, it would be an *ut singuli* action;
- the shareholders can enforce, for themselves, a breach of directors' duties in case they suffered a distinct harm from the company; and
- third parties can also hold a director personally liable in case of a fault separate from their functions, which fault is defined by case law as (i) particularly serious, (ii) intentionally committed and (iii) incompatible with the normal exercise of corporate functions.

It is important to point out that unless one of the directors is solely responsible, directors' liability is collective, and may be joint and several, given the collegial nature of the board. Lastly, the recognition of directors' liability under French law is not that common.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In France, directors and officers can be held liable for criminal and civil charges.

They would be liable for any criminal infringement such as misappropriation of corporate assets, distribution of fictitious dividends or publication of inaccurate annual accounts.

Directors and officers can also be civilly liable if they commit breach of laws and regulations applicable to the company (breach of the by-

laws or other internal regulations). In addition, mismanagement by directors and officers can be a cause for liability if they act contrary to the corporate interest of the company. Mismanagement ranges from negligence to fraud.

Directors and officers can also face administrative and tax liability; for example, in a case where they infringe the AMF securities law-related regulations, the authority is able to impose financial sanctions. In the same way, fraudulent acts or breaches of tax obligations can lead to financial sanctions.

Director and officer liability cannot be restricted or limited on a contractual basis. However, it can be excluded in case the directors and officers demonstrate they acted with a legitimate lack of awareness of a wrongful act or if they show they were in opposition to the decision at stake.

Usually, the company offers insurance to the directors and officers that covers specific defence and investigation costs or damages.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers SA

In SA, the regime of directors' and officers' compensation approval process differs depending on whether the company is listed.

In non-listed SA, the general meeting of shareholders must approve the aggregate amount of the compensation to be paid to the board of directors, as a whole. Then, the allocation of this amount between the directors is decided by the board of directors itself. The board also has exclusive authority to set forth the CEO's compensation scheme and authorise any payment

made to it, without any prior approval required from the shareholders.

CEO's compensation schemes generally include a fixed and a variable portion, the latter being paid upon achievement of targets set by the board.

A listed SA must comply with the say-on-pay procedure (please refer to **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**). Under this regulation, the directors' and officers' compensation schemes are subject to a double approval process from the shareholders:

- the shareholders' general meeting shall approve the compensation policy for the upcoming fiscal year, setting forth the principle and structure of the relevant compensation schemes (ex-ante vote). Any amount paid – or payable – to the directors and/or officers in violation of the approved compensation policy must be void; and
- each year, the shareholders' general meeting shall approve all payments made to directors and officers or amounts owed to them pursuant to the pre-approved compensation policy (ex-post vote). Payment of variable and extraordinary compensation elements shall be subject to the approval of the ex-post vote.

A rejection of the ex-ante vote or of the ex-post vote by the shareholders entails severe consequences:

- if the compensation policy is rejected, the previously approved principles and criteria shall continue to apply or, in the absence of any previously approved policy, the compensation scheme shall be determined in accordance with the compensation attributed

for the previous financial year or, if none, in accordance with existing practice within the company; and

- if the compensation paid – or payable – to the directors and/or officers is rejected, the relevant officer shall be deprived of any variable and exceptional compensation due for the relevant fiscal year.

Compensation schemes of listed companies' officers are also subject to various rules and recommendations, including from corporate governance codes (with for instance increasing recommendation to consider ESG criteria for variable compensation).

SAS

In SAS, the conditions for the compensation of the chairman and members of the board (if any) are set in the by-laws.

SARL

The compensation of the managing directors of the SARL is approved by the shareholders.

4.11 Disclosure of Payments to Directors/Officers

Listed companies must disclose any such compensation in a complete and transparent manner in their Universal Registration Document. This disclosure must provide the total compensation, fixed, variable and exceptional, and benefits of any kind attributed or paid to all corporate officers in the last year.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The company and its shareholders are legally bound by the by-laws, which constitute the main

company's internal regulation. As far as shareholders are concerned, this set of rules, mainly driven by applicable laws of the French Commercial Code, states their specific rights within the company. For instance, their right to vote, their right to receive dividends or their right to information about business and management matters.

In SAS, the importance of the by-laws is even more significant since the relationship between the company and its shareholders mainly relies on them, the SAS corporate form being little regulated by law provisions.

Public disclosure of shareholder information varies depending on the type of company. While SARL are required to disclose shareholder allocations in their by-laws, which can be accessed through public platforms, *sociétés par actions* – such as SAS and SA – do not have a public register of shareholders. Instead, share ownership is recorded internally in share transfer registries maintained by the company. However, for listed companies, the situation differs significantly. Shareholders exceeding certain thresholds must disclose their holdings to both the company and the French Financial Markets Authority (AMF), which then makes this information publicly available.

5.2 Role of Shareholders in Company Management

Shareholders' Involvement

As a general principle, shareholders are not meant to be in charge of the day-to-day management of the company, which is delegated to the corporate officers.

That being said, shareholders are entitled to have an important role in the making of certain decisions – ie, all matters attributed to the gen-

eral meeting by law and the by-laws. For example, the approval of the annual accounts, the appointment and removal of corporate officers and statutory auditors, the amendment of the by-laws or the dissolution of the company.

Besides this “typical” involvement, shareholders now play a more important role as they are increasingly solicited on the management of the company's activity and administration. For example, shareholders are now consulted on the remuneration of executives (say-on-pay) and can also be consulted on the company's action and influence on climate issues (say-on-climate).

No Interference in the Exercise of Executive Functions

Shareholders are not meant to have a direct role in the everyday management of the company, this being reserved to the executive officers who have broad powers to represent the company towards third parties. Therefore, shareholders must refrain from interfering in the executive officer's area of responsibility, otherwise courts may consider such behaviour as a de facto exercise of executive functions and consider the shareholder as a de facto officer (*dirigeant de fait*) accountable like any legal officer (*dirigeant de droit*).

5.3 Shareholder Meetings

Ordinary General Meetings

At least once a year, within six months of the end of the financial year, an annual ordinary general meeting of shareholders must be convened in order to vote on the annual accounts and consolidated accounts, the distribution of dividends and, in listed companies, the compensation of the board members and the executive officers (please refer to **1.3 Corporate Governance Requirements for Companies with Publicly Traded Shares**).

Under the annual ordinary general meeting, shareholders usually also vote on the appointment or removal of board members, the appointment of the statutory auditors, the related-party transactions and any decisions other than those reserved to the extraordinary general meeting of shareholders.

Extraordinary General Meetings

The extraordinary general meeting is competent to approve amendments to the company's by-laws, any changes to the share capital, mergers and spin-offs and the early dissolution of the company.

Shareholders' general meetings are convened by the board or any person designated in the by-laws to do so. Notice for holding meetings must be given at least 15 days in advance in SA and SARL. However, listed companies or companies whose shares are not all held in registered form are required, at least 35 days before the meeting, to publish a notice of the meeting in the Bulletin of Mandatory Legal Announcements (*Bulletin des annonces légales obligatoires*). The notice of the meeting must contain certain mandatory information.

The quorums and majorities required for the validity of meetings vary depending on the ordinary or extraordinary nature of the decision submitted to the shareholders, the corporate form of the company and the provisions of the by-laws.

In SA for instance, adopting an ordinary decision requires a quorum of at least one-fifth of the voting shares on first convocation, no quorum is required on second convocation, and a simple majority of the voting shares of the shareholders present or represented.

The adoption of extraordinary decisions requires a quorum of at least a quarter of the voting shares on first convocation, one-fifth on second convocation, and a two-thirds majority of the voting shares of the shareholders present or represented.

However, it should be noted that increasing the shareholders' commitments towards the company requires a unanimous decision of all the shareholders.

In general, shareholder meetings are held physically at the registered office or any location specified in the notice of the meeting but can also be held remotely or by written consultation if the by-laws provide for it. Under the *Attractivité* Act, shareholder meetings of companies listed on a regulated market are required to be broadcast live, unless technical difficulties prevent or severely disrupt such transmission. Furthermore, these companies must ensure that a recording of the meeting is made available for later consultation and, where applicable, disclose whether the recording encompasses the entire meeting.

5.4 Shareholder Claims

Executive officers and/or directors who violate applicable laws and regulations, the by-laws or who are otherwise at fault in their management are individually or jointly liable towards the company. In this case, one or more shareholders may bring a legal action against the executive officers and directors for damages suffered by the company (action ut singuli). The resulting damages will be paid to the company.

In addition, if the shareholders have suffered personal losses separate from those suffered by the company, executive officers and directors will also be liable to those shareholders (please

refer to 4.9 Other Bases for Claims/Enforcement Against Directors/Officers).

5.5 Disclosure by Shareholders in Publicly Traded Companies

Following the Transparency Directive providing for the harmonisation of transparency requirements across the European Union, French securities laws impose certain strict filing and disclosure requirements to which prospective shareholders in publicly traded companies should pay particular attention.

Such reporting obligations fall primarily within the mandatory disclosure of major shareholdings. The French Commercial Code thus requires the disclosure within four trading days to the issuer and to the AMF of any holding of shares or voting rights when the percentage of such shares or voting rights reaches, exceeds or falls below the following thresholds (whether through open market purchases, negotiated transactions or otherwise): 5%, 10%, 15%, 20%, 25%, 30%, one-third, 50%, two-thirds, 90% or 95%. The AMF then publishes this information. Issuers' by-laws may also impose additional disclosure requirements – even below the 5% statutory threshold – for thresholds of not less than 0.5%.

In addition, upon crossing the thresholds of 10%, 15%, 20% and 25% of the capital or voting rights, the relevant shareholder must also inform the company and the AMF, within five trading days, of its objectives for the following six-month period in a statement of intent (*déclaration d'intention*). In the event of a change in intent within the six-month period following the statement of intent that was originally filed, a new statement must be issued promptly to the company and the AMF and made public under the same conditions. The six-month period is reset with this new statement.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting Legal Reporting

Companies are required to file various documents relating to their accounts for the previous financial year with the registrar of the commercial court. This filing must be made within one month of the approval of the annual accounts by the annual ordinary general meeting, or two months if the filing is made by electronic means.

The filing covers the following documents:

- the annual accounts;
- the management report, in the case of a listed company. For all other companies, the management report does not have to be filed but a copy must be delivered, at the company's registered office, to any person upon request;
- the auditors' report on the annual accounts;
- the proposal for the allocation of profits submitted to the annual general meeting and the relevant resolution on the allocation adopted by the annual general meeting; and
- the consolidated accounts, the group management report and the auditors' report on the consolidated accounts, in the case of a company required to prepare such accounts.

Specific Complementary Filings for Listed Companies

Listed companies are also required to publish and file with the AMF:

- an annual financial report within four months of the end of the financial year; and
- a half-year financial report within three months of the end of the first half of the financial year.

In addition, listed companies have the option of publishing quarterly or interim financial information at their discretion. If they choose to publish such financial information, the AMF recommends that the publication be presented with a commentary designed to clarify the relevant financial information and thus enable investors to better understand the company's situation.

6.2 Disclosure of Corporate Governance Arrangements

Corporate Governance Report

SA and SCA are required to draw up a report on their corporate governance, which is attached to the management report. For listed companies, this report is usually incorporated in the Universal Registration Document.

Corporate Governance Codes

The corporate governance report of listed companies is required to specify, among other things, the corporate governance code applied by the company. In France, the most widely used corporate governance code is the AFEP-MEDEF Code. If the company chooses not to comply with a specific provision of the corporate governance code, it must explain how it departs from it and why, in accordance with the comply-or-explain principle (please refer to **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**). Companies can also choose to refer to the corporate governance code drawn up by Middenext, which is intended for medium-sized companies listed in Paris.

6.3 Companies Registry Filings

In France, companies are registered with the *Registre du Commerce et des Sociétés* (RCS) through the single window for business formalities (*guichet unique des formalités d'entreprises*), which submits the information to the competent commercial court clerk (*greffier du tribunal de*

commerce). Any updates to the constitutive documents during the life of the company must be filed with the relevant companies' registry. These updates and their related corporate documents are publicly available and include amendments to the by-laws, changes to executive officers and board composition, transfers of the registered office, changes to the share capital and statutory auditors.

The financial reports mentioned in **6.1 Financial Reporting** are also required to be filed with the companies' registry. However, micro-enterprises and small companies, as defined in the French Commercial Code, may request confidentiality for their annual accounts from the registry. Following the increase in thresholds by a decree of 28 February 2024, more small businesses will be eligible for this option, reducing administrative burdens and protecting sensitive information.

The registry's clerk has supervisory powers and conducts several checks to ensure compliance with regulations and authenticity of supporting documents. If necessary, the clerk can reject filings or, in some cases, order the company's removal from the registry.

In case of failure to comply with the filing obligations, companies, or their officers in the event the failure constitutes a fault separate to their functions, may be exposed to civil and criminal fines.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The appointment of an external auditor by the shareholders' ordinary general meeting becomes mandatory if, at the end of the financial year, the company exceeds at least two of the following

thresholds (these thresholds have been modified by Decree – 28 February 2024 – transposing a delegated Directive of 17 October 2023) as follows:

- a balance sheet total of EUR5 million;
- net turnover of EUR10 million; and
- 50 employees.

Auditors are subject to certain requirements regarding their independence, which prohibit them from having any personal, financial or professional relationships that are incompatible with the functions of an auditor.

In addition, any commercial activity or paid employment of the auditor for the benefit of the company whose accounts they audit is prohibited in order to preserve the auditor's independence.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Besides the duty of diligence a director must respect, listed companies are required to describe their internal control and risk management procedures in their annual report. They are also legally required to set up an audit committee composed of board members, which must at least include one independent member with specific expertise in financial or accounting matters.

The audit committee is responsible for monitoring the effectiveness of the internal control and risk management systems and of the internal audit of procedures relating to the preparation and processing of financial and non-financial accounting information.

In addition, the audit committee regularly meets with the heads of internal audit and risk control and gives an opinion on the organisation of their departments.

GEORGIA

Law and Practice

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Andersen in Georgia



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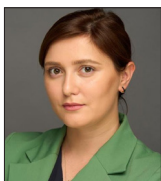
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1. Introductory

1.1 Forms of Corporate/Business Organisations

The principal forms of corporate/business organisations in the Georgian jurisdiction are:

- limited liability company;
- joint stock company;
- limited partnership;
- general partnership;
- co-operative;
- individual entrepreneur.

Limited liability companies and joint stock companies are most widely used. They both provide shareholders with limited liability.

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance requirements for companies in Georgia are provided by statutory provisions or orders/ordinances of various regulatory authorities. The Law of Georgia on Entrepreneurs (adopted on 2 August 2021) is the principal source of law on corporate governance requirements and regulates all forms of business organisations existing in Georgia. Furthermore, the Law of Georgia on

Securities (adopted on 14 January 1999) regulates securities and entities trading on capital markets. A prominent example of a regulatory order is the Corporate Governance Code adopted by the National Bank of Georgia.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with shares that are publicly traded shall be set up with a two-tier board system. Generally, in companies, other than banks, there is no requirement to have independent board members or to observe gender quotas.

Key requirements for such companies include the following.

- Supervisory board – Publicly traded companies shall establish a supervisory board comprising at least three members and not more than 21 members. The supervisory board oversees the activities of the management body and ensures compliance with corporate governance standards.
- Audit committee – Public-interest entities shall establish an audit committee within the supervisory board, which includes at least one independent member. The audit commit-

tee supervises the financial reporting process, the effectiveness of quality control, risk management and the internal audit of financial information.

- Disclosure obligations – Publicly traded companies shall disclose significant information, including financial statements and changes in registered data, to ensure transparency and accountability. This includes the publication of annual accounts, business reports and audit reports.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

As of 2025, there are no major new corporate governance rules or reforms that stand out as particularly topical or transformative in the Georgian jurisdiction. The existing framework under the Law of Georgia on Entrepreneurs and related regulations remains largely stable, with no significant legislative amendments introduced in the area of corporate governance over the past year.

In light of the Russian sanctions regime, which has had and continues to have a far-reaching effect, the banks have been compelled to reassess their internal strategies and decision-making processes to remain compliant with the evolving legal landscape. Additional developments appear likely, particularly as certain Georgian officials are also subject to Western sanctions, a situation that underscores the fluidity of the current sanctions framework and its potential to demand further revisions of the banks' risk management and governance protocols.

As for green or sustainability reporting, there have been no formal regulatory developments or mandates in Georgia to date. While some larger or internationally active companies have

begun to voluntarily incorporate ESG principles into their operations and reporting practices, this remains limited and largely market-driven. There is currently no statutory obligation for Georgian companies to conduct sustainability reporting.

2.2 ESG Considerations

Georgian commercial banks and other financial institutions are required to disclose environmental, social and governance (ESG)-related information in a relevant, useful, consistent and comparable manner. The National Bank of Georgia has developed ESG Reporting and Disclosure Principles. These principles contain detailed guidelines for reporting entities to ensure that their disclosures are fair and comprehensive but concise, strategic, forward-looking and stakeholder-oriented. However, these principles provide non-binding guidelines and do not create additional legal obligations.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The governance and management of a company usually involve the following bodies with the following functions.

General Meeting of Shareholders

The general meeting of shareholders is the highest decision-making body in a company. It is composed of all partners or shareholders and is responsible for making key decisions that affect the company's operations and governance.

Its functions are as follows:

- approving financial reports and annual accounts;

- electing and dismissing members of the management body and supervisory board;
- making decisions on the distribution of profits and dividends;
- approving amendments to the charter or instrument of incorporation;
- deciding on the reorganisation or winding-up of the company; and
- authorising significant transactions and changes in capital.

Management Body/Board of Directors

The management body/board of directors is responsible for the day-to-day operations and management of the company. It can consist of one or more managers who are appointed by the general meeting.

Its functions are as follows:

- managing the company's business activities and operations;
- representing the company in relations with third parties;
- making decisions on issues that do not fall within the authority of the general meeting or supervisory board;
- ensuring compliance with legal and regulatory requirements; and
- preparing and submitting financial statements and business reports.

Supervisory Board

The supervisory board oversees the activities of the management body and ensures that the company adheres to good governance practices. Generally it is not mandatory for a company to have a supervisory board; it is mandatory only for public-interest entities and companies with publicly traded shares.

Its functions are as follows:

- controlling and supervising the activities of the management body;
- reviewing and approving the annual accounts and business reports;
- representing the company in legal disputes against managers; and
- convening the general meeting when necessary.

The management structure may be one- or two-tier.

- One-tier structure – In this model, the company's management is undertaken by managers or directors forming a single management body. This structure blends the management and oversight functions, with these individuals directly overseeing the company's operations.
- Two-tier structure – Distinguished by a division of roles, the management tasks in a two-tier structure are carried out by one or more managers. Simultaneously, the supervisory board is responsible for overseeing the company's strategic direction, ensuring alignment with laws and the company charter. Unlike managers, the supervisory board does not engage in day-to-day management but oversees the managers' activities without issuing binding directives.

Managers in both structures are endowed with the authority to make decisions concerning daily operations. They, along with the supervisory board members in a two-tier system, are bound by fiduciary duties to prioritise the company's best interests.

3.2 Decisions Made by Particular Bodies

The general meeting of shareholders typically decides issues material to the operation and

governance of the legal entity. It holds specific exclusive powers, such as the following:

- amendment of company charter;
- company liquidation or reorganisation;
- approval of financial reports and annual accounts;
- election and dismissal of managers and supervisory board members;
- increase or reduction of company's capital; and
- distribution and payment of dividends.

The management powers can be divided between the two boards – the board of directors and supervisory board.

Any executive decision may be made by the board of directors. The directors are further empowered to represent the company before third parties. If the company has established a two-tier structure, it is likely that some material agreements and material decisions will be subject to approval of the supervisory board. The supervisory board can appoint and dismiss directors. In the one-tier structure, this power lies with the general meeting of shareholders.

3.3 Decision-Making Processes

General Meeting of Shareholders

The decision-making process is as follows.

- Agenda – The agenda of the general meeting is prepared and distributed to all partners or shareholders at least 14 days before the meeting.
- Quorum – The general meeting is authorised to adopt decisions if attended by partners holding a majority of votes (if not otherwise defined by the charter of the company). If the quorum is not met, a reconvened meeting can

adopt decisions irrespective of the number of attending partners.

- Voting – Decisions are made by a majority of votes unless a higher threshold is specified by the charter or the law.
- Minutes – The minutes of the general meeting are drawn up within 15 days after the meeting and include details of the decisions made, voting results and any objections raised.

Ordinary general meetings of the shareholders shall be convened at least once a year.

A director or a shareholder or a group of shareholders holding at least 5% of the outstanding shares may call an extraordinary general meeting.

Board of Directors

The process is as follows.

- Meetings – The management body holds regular meetings to discuss and make decisions on operational matters. The frequency and procedures for these meetings are determined by the charter.
- Quorum and voting – Decisions are made by a majority of votes of the members attending the meeting. If votes are equally divided, the vote of the chairperson is decisive.
- Documentation – Decisions made by the management body are documented and communicated to relevant stakeholders as necessary.

Supervisory Board

The process is as follows.

- The supervisory board must include at least three members. In public-interest entities, it must include at least one independent member.

- Members of the supervisory board are elected by the General Meeting for a term of not more than three years.

Sessions of a board of directors and a supervisory board are subject to regulation under the company's charter. Decisions are usually made by half of the board members. There are no mandatory rules in this respect and regulation of board sessions and decision-making are within the company's discretion.

4. Directors and Officers

4.1 Board Structure

Boards of directors may be composed of any number of directors. The number of members of the board of directors is determined by the company's charter. The members of the board of directors shall be elected for a period of not more than three years, although they can be re-elected.

4.2 Roles of Board Members

Each member of the board of directors has the same role. There are no differences among individual board members. Although companies may wish to assign specific titles to directors, such as finance director, operational director, etc, this will not affect their voting power or responsibility before the company.

If a company's management body consists of multiple members, they shall exercise representative authority jointly, unless the charter provides otherwise – such as authorising individual representation by one or more members, joint representation by certain members, etc.

4.3 Board Composition Requirements/Recommendations

In commercial banks, the Corporate Governance Code mandates gender diversity and independent directors. Moreover, board members are required to fulfil qualification requirements. There are no requirements for legal entities other than commercial banks.

4.4 Appointment and Removal of Directors/Officers

Directors are usually appointed and removed by a decision of the general meeting. In two-tier structures, this power lies with the supervisory board. Directors may be dismissed at any time without cause. Any agreement that contradicts this provision is considered void.

There are certain restrictions on who may be appointed as a director or officer of a company. For instance, a member of the supervisory board of a joint stock company cannot simultaneously be a member of the management body of the same company. Additionally, the company charter may provide for a list of positions that cannot be combined with the role of a member of the supervisory board. In regulated entities, especially within the financial sector, individuals proposed for appointment as directors or officers must not only meet standard legal and fiduciary obligations but also satisfy specific suitability and qualification requirements imposed by the relevant regulatory authorities.

4.5 Rules/Requirements Concerning Independence of Directors

The corporate governance code applicable to financial institutions defines directors' independence as their ability to function objectively and independently without influence or potential influence from any third parties.

Directors who have a conflict of interest should disclose such interest and abstain from voting. A director may be deemed to be an interested person if they or persons related to them, in the case of the entry into a transaction by a public company or its subsidiary (a company in which the reporting company holds more than 50% of shares), meet one of the following conditions. The person:

- is the other party to the transaction;
- directly or indirectly holds 20% or more of the total number of votes of the other party to the transaction;
- is a member of the governing body of the other party to the transaction;
- is appointed/elected as a member of the governing body of the reporting company upon the proposal of the other party to the transaction or of the holder (holders) of 20% or more of the total number of votes of the other party to the transaction;
- receives monetary or any other benefits on the basis of the transaction, which are not related to the ownership of shares in the reporting company or to membership of the governing body; or
- is considered an interested person under the charter of the reporting company.

Conflict of interest cases may be further regulated by the company charter as well as the service agreement concluded with the director.

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors and officers of a company are as follows.

- **Duty of care** – Act diligently and in good faith, like a prudent manager, and liable for harm caused by negligent or intentional breaches.

- **Duty of loyalty** – Respect the rights of the company and all partners equally, avoiding actions that harm the company or its stakeholders.
- **Avoiding conflicts of interest** – Disclose personal interests in transactions and cannot vote on related matters. Certain transactions require prior approval.
- **Acting within authority** – Operate within the legal and statutory limits of their role and follow decisions of authorised company bodies.
- **Insolvency filing** – File for insolvency within three weeks if the company becomes insolvent, to protect creditors' interests.
- **No misuse of opportunities** – Cannot exploit company-related business opportunities for personal or third-party gain without consent, even for up to three years post-dismissal.
- **Non-competition** – Cannot engage in competing activities or manage a competing company without consent, for up to three years after leaving the role.

The directors and the members of the supervisory board shall conduct the company's business in good faith. In particular, they shall take care as an ordinary person of sound mind in a similar capacity and under similar circumstances would, acting in the belief that their action is in the best interest of the company. If directors fail to fulfil the above obligation, they shall be jointly and severally liable for damages incurred by the company. Moreover, while managing the company, directors shall not have personal interests that conflict with the interests of the company. Directors shall not be entitled to make decisions in accordance with their interests or interests of related persons with respect to the opportunities of the company. In the event of conflict, the interest of the company shall prevail.

4.7 Responsibility/Accountability of Directors

The directors owe their duties to the company. This encompasses acting in the best interests of the company as a whole, which includes considering the interests of its shareholders. In some cases, directors may be required to comply with the instructions of shareholders. However, their primary duty is still owed to the company and, if following the shareholders' instructions they damage the company's interests, the directors will be liable for breach of duty. The directors must conduct the company's business with the diligence of a manager in good faith, acting with the care that an ordinary person of sound mind would exercise under similar circumstances. This duty of care ensures that directors act in the best economic interests of the company.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Breach of director's duties can be enforced by the company directly or by its shareholders acting derivatively by filing a derivative suit. In particular, one or more shareholders can initiate legal action to require directors to compensate for damage inflicted on the company. This includes claims for the transfer of any profit earned from transactions conducted on behalf of the directors or third parties. Shareholders are considered eligible claimants if they have requested the company to file a lawsuit and the company has not acted within 90 days, or if waiting for this period would cause irreparable harm to the company. If a court rules in favour of the shareholders, the company must reimburse the shareholders for reasonable expenses related to the lawsuit.

Directors who breach their duties are liable for any damage incurred by the company. They may be required to compensate for the damage or

transfer any profit earned from transactions conducted on behalf of themselves or third parties to the company. The liability for intentional failure to fulfil the duty of good faith cannot be limited by the charter or the shareholders' decision.

In cases of breach of duties, directors can be dismissed from their position immediately by the general meeting or the supervisory board, depending on the company's structure.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other bases for claims or enforcement against directors or officers for breaches of corporate governance requirements may be contractual. Companies usually sign service agreements with their directors and officers. Those agreements will set out the director's obligations as well as their liabilities. The agreements may also envisage penalties. The company may rely on the agreement to seek compensation for its breach. The same agreement may limit the director's liability to a specific sum. Although not common, a director's liability insurance may also be procured.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

No approvals are required in connection with the remuneration, fees or benefits payable to directors and officers. The director's remuneration is usually set by the general meeting of shareholders. Reporting entities and entities trading on stock markets will likely have adopted a remuneration policy. They may even have a remuneration committee in their supervisory board.

4.11 Disclosure of Payments to Directors/Officers

A company does not have to make disclosures in relation to the remuneration, fees or benefits payable to directors and officers.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

This relationship is primarily defined by the rights and obligations of shareholders, the structure of company management, and the mechanisms for shareholder participation in company decisions envisaged under applicable law or the charter of the company.

Shareholders have several key rights, including the right to participate in general meetings, vote on important company matters, receive dividends, and access company information. They also have the right to dispose of their shares freely, unless otherwise restricted by the company's charter.

Shareholders are obligated to make contributions for their shares and provide updated information to the company or the licensed securities registrar. They must also comply with any additional duties specified by law or the company charter.

As a general rule of limited liability, shareholders of a joint stock company and of a limited liability company shall not be liable for the obligations of the company. However, shareholders of a joint stock company and of a limited liability company shall be liable if they abuse the rule of limited liability, in which case their joint and unlimited liability for the company obligations may be determined by the competent court.

The data registered with the Registry (as defined below), including information on shareholders in relation to the limited liability companies, is public. Any person has the right to access this data and obtain an extract from the registration authority. Electronic copies of the documents submitted during the registration process are published on the central electronic platform of the registration authority and are available for free. Information about shareholders in joint stock companies is not public and cannot be accessed through the Registry's data. These companies maintain their own shareholders' registry as an internal document, which is available only upon request. A joint stock company with more than 50 shareholders must maintain its shareholders' register through a licensed securities registrar.

5.2 Role of Shareholders in Company Management

Shareholders can be actively involved in the management of a company. As a rule, they adopt material decisions regarding the company, such as its reorganisation, liquidation and decisions relating to its capital. However, the shareholders may wish to undertake a more active role in the management. In such a case, the charter may envisage operational decisions that cannot be taken without shareholder approval, such as the following:

- investments;
- taking out loans;
- selling the company's business; and
- certain transactions with a value higher than a specific threshold.

The shareholders are able to direct the management of a company to take, or refrain from taking, certain actions in the business. However,

directors may refuse such instructions if they do not benefit the company's interests.

5.3 Shareholder Meetings

Shareholder meetings are required unless a unanimous written decision is taken by all shareholders. For the rules that govern the holding and conduct of such meetings, see 3.3 Decision-Making Processes.

5.4 Shareholder Claims

Shareholders may have several claims against the company or its directors, as follows.

- Breach of duty – Directors must act with diligence and good faith. Shareholders can claim for damages if directors fail to fulfil their duties.
- Conflict of interest – Directors must disclose any conflicts of interest and obtain approval for related transactions. Shareholders can claim for damages if these rules are violated.
- Material transactions – Consent from the supervisory board or general meeting is required for transactions involving 25% or more of the company's assets. Shareholders can void transactions if procedures are violated.
- Abuse of dominant influence – Dominant shareholders abusing their influence can be held liable for damages to the company or other shareholders.
- Right to information – Shareholders can request company information and inspect documents. If refused, they can appeal to a court.
- Redemption of shares – Shareholders can require the company to redeem their shares at a fair price if a decision substantially impairs their rights or involves reorganisation.

If a director breaches any of the fiduciary duties, a shareholder may launch a derivative suit on behalf of the company and seek from the director reimbursement of damages to the company.

5.5 Disclosure by Shareholders in Publicly Traded Companies

There are no direct disclosure obligations on shareholders in publicly traded companies. However, in regulated entities any acquisition or transfer of shares may be subject to regulatory approval. Moreover, ultimate beneficial ownership information shall be supplied to commercial banks and insurance providers.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

In accordance with Georgian legislation, companies must prepare and submit reports to the regulatory authorities annually, by October 1st of the year following the reporting period.

The financial statements include the following forms:

- balance;
- report about income and material losses;
- explanations on the movement of funds in the accounts of the organisation;
- annual results of the economic activity of the company;
- current financial position; and
- explanatory note.

6.2 Disclosure of Corporate Governance Arrangements

Disclosures on corporate governance arrangements in financial reports usually follow the reporting standards. Georgia uses International

Financial Reporting Standards (IFRS) for financial reporting.

In addition, major decisions, such as amendments to the charter, reorganisation and dividend distribution, must be approved by the general meeting and documented. Information about the composition of the supervisory board, including the election of the chairperson and any changes, must be disclosed.

The management body is required to prepare annual accounts and a business report, including a proposal for using net profit, and submit them to the supervisory board and general meeting for approval. These documents must be published on the company's website (if any) at least one week before the annual meeting and displayed at the company's office.

6.3 Companies Registry Filings

In Georgia, the National Agency of Public Registry, under the Ministry of Justice (the “Registry”), is responsible for the incorporation and registration of companies. Companies must file an incorporation agreement, which includes the company's charter and essential data such as the company name, legal address, and identification data of each shareholder. A separate written consent from individuals with management and representative powers must also be submitted unless included in the incorporation agreement. An application for registration, signed by authorised persons and accompanied by necessary documents, is also required. Any changes in registered data, such as amendments to the charter or changes in the management body, must be registered with the Registry.

The data registered with the National Agency of Public Registry is public, and any person can access this data and obtain an extract. Elec-

tronic copies of registration documents are published on the central electronic platform and are available for free.

Failing to make the required filings can result in the suspension of registration, restricting the company's representative powers, property disposal rights, tax operations, bank account management and credit access. Continued non-compliance can lead to the revocation of the company's registration and subsequent liquidation. The management body may also face administrative liability for failing to fulfil disclosure obligations.

The Registry has supervisory powers to ensure compliance with registration requirements. It verifies compliance, identifies defects in registered data, and grants the status of a company with a defect, suspending the validity of the registered data until the defect is remedied. The registration authority must be informed of any changes in registered data and is responsible for publishing electronic copies of registration documents and ensuring public access to this information.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Certain reporting companies (such as commercial banks) must appoint external auditors in connection with their financial statements. Their names must be disclosed. The right to appoint the external auditor is reserved to the general shareholders' meeting. External auditors are allowed to provide non-auditing services and this might undermine their independence. Rotation of the external auditor is not required.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Requirements prescribed by Georgian law in relation to directors in connection with the management of risk and internal controls in the company are provided in 4.6 Legal Duties of Directors/Officers, 4.8 Consequences and Enforcement of Breach of Directors' Duties and 4.9 Other Bases for Claims/Enforcement Against Directors/Officers.

GERMANY

Law and Practice

Contributed by:

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POELLATH



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POELLATH is an internationally operating German law firm of more than 180 lawyers and tax advisers in Berlin, Frankfurt and Munich, providing high-end legal and tax advice. The firm advises on all transaction-related areas, including corporate, M&A, private equity, funds, real estate, private clients, succession planning and tax-related matters. **POELLATH's** corporate advice includes corporate law and group company law, reorganisations, capital market rules, corporate litigation and compliance. **POELLATH** advises publicly listed and private companies on preparing and conducting their general and

shareholder meetings on all matters, including mergers, spin-offs and hive-downs, conversions of legal form, and on all corporate advisory matters related to corporate governance. A further core area is public takeovers with subsequent corporate integration. Key clients include Vodafone, Deutsche Telekom AG, shareholders of Porsche Automobil Holding SE, PUMA SE, Wacker Neuson SE, Eckert & Ziegler SE, Nemetschek SE, Münchener Hypothekenbank, BayWa, Giesecke+Devrient, Fiege Group, Groz-Beckert and STAEDTLER.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

German law differentiates between capital companies and partnerships. The following chapter will focus on capital companies, as these are the most important and regulated forms of companies in Germany.

Capital Companies

Capital companies are legal entities where the liability is limited to the assets of the company – ie, the shareholders' liability is limited to what they have invested in the company. The most common legal forms of capital companies are the limited liability company (*Gesellschaft mit beschränkter Haftung* or GmbH) and the stock corporation (*Aktiengesellschaft* or AG). Other forms of capital companies are the European stock company (*Societas Europaea* or SE) and the partnership limited by shares (*Kommanditgesellschaft auf Aktien* or KGaA).

The KGaA is a capital company, but also has some elements of a partnership.

Partnerships

Partnerships are characterised by the personal liability of the partners. The most popular legal

form of a partnership is the limited partnership (*Kommanditgesellschaft* or KG), consisting of limited partners whose liability is limited to a certain amount agreed and disclosed in the commercial register, and general partners with unlimited liability. However, the general partner may have the legal form of a capital company, thereby limiting its liability.

German law also acknowledges the partnership under civil law (*Gesellschaft bürgerlichen Rechts* or GbR) and the general partnership (*Offene Handelsgesellschaft* or OHG), with unlimited liability of their partners.

1.2 Sources of Corporate Governance Requirements

The primary sources for corporate governance requirements for capital companies in Germany (GmbH, AG, KGaA, SE) are:

- the German Limited Liability Companies Act (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung* or GmbHG);
- the German Stock Corporation Act (*Aktiengesetz* or AktG);
- the European and German acts on SEs (in particular the European SEVO and the German SEAG);

- the German Commercial Code (*Handelsgesetzbuch* or HGB);
- the Reorganisation of Companies Act (*Umwandlungsgesetz* or UmwG);
- the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz* or WpÜG);
- the Market Abuse Regulation (*Marktmissbrauchsverordnung* or MAR); and
- the Securities Trade Act (*Wertpapierhandelsgesetz* or WpHG).

Beyond this, the German Corporate Governance Code (Deutscher Corporate Governance Kodex or DCGK) sets out further corporate governance rules for listed companies, which differentiate between recommendations and suggestions. In 2020, the DCGK introduced the category of principles which precede the recommendations and suggestions regarding a certain subject matter and outline the fundamentals of the applicable law.

In 2022, the DCGK was amended, substantiating some ESG aspects as well as the guidelines on internal controlling in response to new legislation on financial integrity.

Moreover, non-governmental regulations such as applicable listing rules enacted by the stock exchanges also establish corporate governance requirements.

Certain industry sectors (eg, banks) are subject to further regulation with respect to, inter alia, their corporate governance.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Shares of an AG, SE and, less commonly, a KGaA may be listed on a stock exchange. The primary

source for corporate governance requirements concerning listed AGs and KGaAs, as well as (to a lesser degree) SEs, is the AktG, as it differentiates between rules for listed and non-listed companies. Its requirements are mandatory. The HGB, WpHG, WpÜG, the European and German Securities Prospectus rules (the European WPVO and the German WpPG), the Stock Exchange Act (*Börsengesetz* or BörsG) and the MAR provide for further mandatory regulation in relation to, inter alia, listed companies' corporate governance.

To promote a high corporate governance standard, the DCGK contains corporate governance standards in the form of recommendations and suggestions for listed companies with a two-tier corporate governance system; however, the rules of the DCGK shall also be applied correspondingly by listed companies with a single-tier corporate governance system (see **3.1 Bodies or Functions Involved in Governance and Management**). The DCGK is not enacted by the legislature, but by the German Corporate Governance Commission and is therefore not a statute or an ordinance, but rather “*soft law*”, so the standards set in the DCGK are principally voluntary. Recommendations shall be complied with and, if not, deviations have to be explained and disclosed (the principle of “*comply or explain*”) in a declaration of compliance (*Entsprechenserklärung*), to be resolved upon annually by the responsible corporate governance bodies of the listed company.

The declaration of compliance is to be included in the declaration on corporate governance, which itself is part of the management report. The issuance of the declaration of compliance is obligatory. Deviations from suggestions are allowed without disclosure. In practice, listed companies seek to comply with the standards

set out in the DCGK, in particular the recommendations.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance Sustainability, ESG and Supply Chain

The topic of sustainability as well as social and environmental responsibility has become increasingly significant in both German and global corporate governance, resulting in more specific and extensive expectations and legislation on this matter, both at national and EU level. In particular, the EU Corporate Sustainability Reporting Directive (CSRD) as well as the German Supply Chain Act came into force in January 2023 (see **2.2 Environmental, Social and Governance (ESG) Considerations**).

Cross-Border Conversion

The Conversion Directive Implementation Act was adopted in early 2023. In summary, it provides a harmonised legal framework for cross-border conversions, mergers and divisions at EU level.

Financing for the Future Act

With effect from 15 December 2023, the Financing for the Future Act introduced numerous changes for stock corporations. It aims to make it easier for companies, especially start-ups, to access the capital markets. Shares with multiple voting rights were reintroduced in the Stock Corporation Act. Additional structuring options were also introduced to simplify capital increases with the exclusion of subscription rights.

EU Listing Act

As part of the EU Listing Act, changes to capital market law are expected to be implemented in the first half of 2024. These include amendments

to the MAR (eg, changes to ad hoc disclosure of insider information by listed companies) and the EU Prospectus Regulation.

2.2 ESG Considerations HGB

Under the HGB, larger listed capital companies with more than 500 employees are under a duty to issue a non-financial declaration that expands their management report. This declaration has to briefly describe the business model of the company. Moreover, it has to refer to other aspects of corporate social responsibility – at least to environment-related, employee-related and social matters as well as to the respect shown for human rights and the efforts made to fight against corruption and bribery.

CSRD

In January 2023, the new CSRD came into force at the EU level. The goal was to bring corporate sustainability reporting in line with the EU's ambition to become the first climate-neutral continent by 2050. The new CSRD expanded the reporting requirements to include further information on environmental, social and governance matters in addition to the already-known aspects concerning environmental, labour and social matters, respect of human rights and the fight against corruption and bribery.

The new CSRD was to apply to all companies listed on a regulated EU market and non-capital-market-oriented companies that exceed two of the following three criteria:

- EUR50 million annual turnover;
- EUR25 million balance sheet total; and
- an average of at least 250 employees.

However, as the directive has not yet been implemented into German law, the new reporting

requirements do not apply. In February 2025, the EU Commission announced that the scope of application will be decreased significantly. Thus, if and to what extent the directive will come into force in Germany is unclear.

Further, the Act on Corporate Due Diligence Obligations in Supply Chains came into force in January 2023 and was expanded as of January 2024, intending to implement the UN Guiding Principles on Business and Human Rights throughout the global supply chain. The EU Corporate Sustainability Due Diligence Directive (CSDDD) came into force in July 2024 and is to be implemented into German law by July 2026. Also, in respect of this directive, the EU Commission announced that the directive will be amended in a fundamental way.

In June 2021, the federal government passed the so-called Supply Chain Act (*Lieferkettensorgfaltspflichtengesetz*), which obliges companies to respect human rights as well as the environment throughout the global supply chain, and to remedy violations. For this purpose, companies must establish an appropriate risk-management system and conduct a risk analysis for themselves and suppliers. The first is ensured by the appointment of an internal officer for monitoring the system. Additionally, companies must establish a procedure for filing complaints concerning human rights violations. Finally, companies must publish an annual report on their compliance containing fulfilment of their obligations under the Supply Chain Act. The law came into force on 1 January 2023, for companies in Germany with at least 3,000 employees. As of 1 January 2024, the new regulations apply for companies with at least 1,000 employees.

However, the parties of the new federal government set out in a coalition agreement (*Koali-*

tionsvertrag) published on 9 April 2025 that the Supply Chain Act is to be omitted. The intention is to replace the Supply Chain Act with a law on international corporate responsibility that implements the CSDDD in a low-bureaucracy and enforcement-friendly manner. It is further intended to abolish the reporting obligation under the Supply Chain Act. Furthermore, violations of the existing statutory due diligence obligations – with the exception of massive human rights violations – are not to be sanctioned until the new law comes into force.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management Management Board

The predominant board structure of an AG and an SE follows the two-tier corporate governance system, with a management board (*Vorstand*) managing and representing the company, and a supervisory board (*Aufsichtsrat*) supervising the management board, in each case accompanied by the third corporate body, the general meeting (*Hauptversammlung*). The management board manages the company under its own responsibility and at its own discretion. It is not subject to any instructions from the supervisory board or the general meeting.

However, the management board is subject to the prior approval of the supervisory board for certain business transactions and measures, either foreseen in the articles of association of the company or by the supervisory board itself – eg, in the rules of procedure for the management board.

Administrative Board

A single-tier corporate governance system with one board primarily known in other jurisdictions is only allowed in Germany within an SE. The board is called the administrative board (*Verwaltungsrat*), and consists of executive and non-executive board members. The administrative board is responsible for the management and supervision of all material company matters (*Oberleitung*) as well as the determination of guidelines for the SE's business, and appoints managing directors (*Geschäftsführende Direktoren*), who are responsible for the day-to-day management of the company.

The managing directors may be members of the administrative board if and to the extent that the majority of the members of the administrative board continue to be non-executive. The administrative board is entitled to issue internally binding instructions to the managing directors.

General Partner

The peculiarity of a KGaA is that the general partner is responsible for the management. The general partner, being a shareholder of the KGaA, may be one or more natural persons or, more common in practice, a capital company itself – eg, a GmbH, AG or SE. The corporate governance system of such a capital company is to be differentiated from the corporate governance of the KGaA.

The corporate governance of the general partner company follows the principles applicable to the corporate form that company takes. The KGaA has in any case a supervisory board that is responsible for the supervision of the management, but in the case of a capital company as general partner it is responsible for neither the appointment, dismissal and service contracts of

the management of the general partner nor for the determination of the financial statements.

The general meeting of an AG, SE and KGaA has no corporate governance powers.

Managing Directors

A GmbH generally has managing directors (*Geschäftsführer*) and the shareholders' meeting (*Gesellschafterversammlung*), but no statutorily required supervising body. The managing directors are responsible for the management and representation of the company. In principle, they decide autonomously.

However, the shareholders' meeting is – in contrast to the situation in an AG – the supreme decision-making body of the GmbH, and has the authority to issue internally binding instructions to the managing directors. In a GmbH, a voluntary supervisory or advisory board may be implemented. Apart from this, a supervisory board is to be installed only in the case of codetermination (see **4.1 Board Structure**).

3.2 Decisions Made by Particular Bodies Management Board

In an AG and a two-tier system SE, the management board responsible for the management of the company decides on any and all business transactions and measures within and outside the ordinary course of business under its own responsibility and discretion. However, material measures within and measures outside the ordinary course of business are subject to the prior approval of the supervisory board. For this purpose, applicable law provides that a catalogue containing those approval rights has to be established, either by the general meeting in the articles of association or, alternatively and – in practice – more relevant, by the supervisory board itself in the rules of procedure for the

management board, which is an important part of supervising the management board.

Besides the supervision of the management board, the supervisory board is responsible for:

- the appointment and dismissal of the members of the management board;
- their service contracts; and
- the review and determination of the financial statements.

Administrative Board

In a single-tier system SE, the administrative board is responsible for fundamental management issues, such as long-term business goals, the organisational structure, and the strategy and general guidelines of the SE, as well as the budgeting; whereas the managing directors are “only” responsible for the day-to-day management. The administrative board has the authority to issue internally binding instructions to the managing directors.

General Meeting

Only selected decisions are reserved by law for the general meeting of an AG and an SE. With respect to the annual ordinary general meeting, such decisions include the appropriation of profits, the appointment of the auditor, the formal approval of action for members of both the management board and supervisory board, and the vote on the annual remuneration report; Fundamental, extraordinary decisions include:

- the election and removal of the supervisory board members;
- amendments to the articles of association; and
- resolutions on restructuring measures and the sale of substantially all of the corporation’s

assets, as well as on corporate agreements (profit and loss pooling agreements).

Managing Directors

Managing directors of a GmbH can principally make day-to-day management decisions without consulting the shareholders. However, as the shareholders’ meeting is the supreme body, a broader catalogue of decisions is reserved by law for the shareholders’ meeting of a GmbH than for a general meeting of an AG: all decisions that the ordinary general meeting of an AG has to take plus the review and determination of the financial statements and all fundamental, extraordinary decisions of the general meeting of an AG, as well as the right to instruct the managing directors.

3.3 Decision-Making Processes Management Board

The management board of an AG and a two-tier system SE generally decides in physical or virtual meetings, if a certain quorum of – most of the time – more than half the members of the management board are present or represented, by way of resolution, generally to be passed by a simple majority. However, qualifying majority requirements can be set – eg, in the rules of procedure for the management board. In practice, it is recognised and common that members of the management board are allocated certain individual responsibilities as part of their department (*Ressort*).

Decisions within each department are made by the responsible, single member of the management board, unless such decision is of material nature, in which case a resolution of the management board is necessary. This also applies where another member of the management board so requests. Finally, the management board may

form committees for specific tasks, although this is not that common in practice.

The same decision-making process applies (more or less) to managing directors of a single-tier system SE and a GmbH.

Supervisory Board

The supervisory board of an AG, a two-tier system SE and a KGaA decide by way of resolution, generally with a simple majority. However, the articles of association or the rules of procedure for the supervisory board may foresee qualifying majority requirements. Supervisory board meetings shall be held as physical meetings from the statutory starting point.

Virtual meetings as well as hybrid forms are permissible. Supervisory board members not present in a meeting may not be represented by third persons or other supervisory board members, but can only give a written voting declaration (*Stimmbotschaft*). The meeting has a quorum if the majority of members are present – at least three.

The supervisory board is entitled to form committees from within itself – eg, an audit committee and a nomination committee. The DCGK expressly requires the formation of these two committees for listed companies. Committees are generally responsible for preparing supervisory board topics and consummating resolutions passed by the supervisory board. Sometimes, committees are also entitled to resolve instead of the supervisory board. However, this is not allowed in statutorily foreseen topics – eg, decisions concerning the remuneration and service contracts of members of the management board. Rules applying to the supervisory board in a two-tier system also have to be adhered to

by the administrative board in a single-tier system SE.

4. Directors and Officers

4.1 Board Structure

Management Board

There is no legally predefined structure for the management board of an AG or two-tier system SE, nor for the managing directors of a single-tier system SE or GmbH. The management board can consist of one or more natural persons, unless the articles of association require a minimum number of members; the same applies to the number of the managing directors.

Supervisory Board

The supervisory board of an AG, KGaA and a two-tier system SE, and the administrative board of a single-tier system SE, has to consist of at least three members, or a higher number up to nine, 15 or 21 members, depending on the registered share capital of the corporation, to be set in the articles of association.

If an AG, KGaA or GmbH exceeds the threshold of, generally, 500 German employees, one third of the supervisory board members of the company must be employee representatives – ie, the one-third participation (*Drittelbeteiligungsgesetz* or *DrittelbG*). In this case, the number of supervisory board members must be divisible by three. If an AG, KGaA or GmbH and its controlled companies exceed, generally, 2,000 German employees in total, the supervisory board must consist of 50% employee representatives – ie, the parity codetermination (*Mitbestimmungsgesetz* or *MitbestG*). In this case, the supervisory board must consist of at least 12 members, with the exact number increasing depending on the total number of German employees.

German codetermination rules do not apply to the SE. Instead, when incorporating an SE, an agreement on the participation of employees in the SE (the so-called employee participation agreement) has to be negotiated with the special negotiating body, which is established particularly for such negotiation, representing employees from the German company, its subsidiaries and branches that are in EU and EEA member states other than Germany. The rules on codetermination are part of the agreement, with the general principle that the level of codetermination of the German company used to incorporate the SE shall be maintained (freezing of codetermination prior to and after principle) – eg, if no codetermination exists and needed to exist prior to the incorporation of the SE, then no codetermination would need to be agreed upon in the employee participation agreement for the SE, etc.

4.2 Roles of Board Members

The applicable law does not predefine roles for members of the managing bodies. One member of the management board can be and usually is nominated as chairman or spokesperson. Apart from this, it is common for the tasks and duties of the management board and managing directors to be divided between them in several departments, either functional or operational divisions. Thereby, names like CEO, CFO and COO are generally attached to the members on their business cards, the website, and in the email footer; however, these are neither statutorily foreseen nor do they trigger any special further rights or obligations.

With respect to the supervisory board of an AG, and a two-tier system SE or an administrative board of a single-tier system SE, only the following rules have to be considered. Generally, each member has the same rights and duties,

and must be familiar with the relevant business sector of the company. However, according to applicable law, boards of listed companies must have two members with certain skills, one with accounting expertise and the other with auditing expertise.

4.3 Board Composition Requirements/ Recommendations

Management Board/Managing Directors

Beyond the requirements set out in **4.1 Board Structure** and **4.2 Roles of Board Members**, there are no other statutory rules governing the composition of the management board of an AG or a two-tier system SE, nor of the managing directors of a single-tier system SE or GmbH. However, if such a company is listed on a stock exchange as well as parity codetermined and consists of more than three members as of 1 August 2022, at least one new member must be female and one must be male.

With respect to the management board of an AG, and a two-tier system SE or an administrative board of a single-tier system SE, that is listed on a stock exchange or codetermined, the supervisory board must determine a target percentage for women on the management board and the management boards for second/third line management, as well as deadlines for when such percentages are to be reached. In the case of a set target of zero, the management board must justify this in a clear and comprehensive manner. If at the time of the determination the percentage of women on the management board is below 30%, the target percentage may not be lower than the present percentage.

These corporations must include a declaration on corporate governance in their management reports. The DCGK recommends taking diversity into account when composing the management

Composition of Supervisory Boards

In AGs, SEs and KGaAs that are parity code-terminated and listed on a stock exchange, the supervisory board (or, in the case of a single-tier system SE, the administrative board) must be composed of at least 30% women and at least 30% men. The minimum percentage must be complied with by the shareholder and employee representatives on the board in its entirety. Furthermore, corporations that need to fulfil the aforementioned gender criteria must include information on whether the company has complied with the portion requirements for the appointment of women and men as supervisory board members in their declaration on corporate governance.

With respect to the supervisory board of an AG, and a two-tier system SE or an administrative board of a single-tier system SE, that is listed on a stock exchange or codetermined, the supervisory board must also set a target for women on the supervisory board as well as deadlines by when such a target is to be achieved. With regard to a target of zero or below 30%, the same applies to the supervisory board as to the management board as described above.

At least one member of the supervisory board must have expertise in the field of accounting and at least one other member of the supervisory board must have expertise in the field of auditing. Sufficient expertise can, for example, be assumed for:

- financial directors;
- expert employees from the fields of accounting and controlling analysts; and
- long-standing members of audit committees or works council members who have acquired this ability in the course of their work through further training.

The DCGK recommends, among other matters, that the supervisory board determines concrete objectives regarding its composition and prepares a profile of skill and expertise for the entire board while taking diversity into account. The profile of skill and expertise shall also comprise expertise regarding sustainability issues.

It is recommended that both are taken into account for the supervisory board's proposals to the general meeting. The DCGK further recommends that a certain number of members of the supervisory board as well as certain members – eg, the chairperson – are independent (see 4.5 Rules/Requirements Concerning Independence of Directors). The implementation status of the objectives and the profile of skill and expertise as well as the number of independent members deemed to be appropriate by the supervisory board are to be disclosed in the corporate governance report in the form of a qualification matrix.

4.4 Appointment and Removal of Directors/Officers

In an AG and an SE, the respective supervisory or administrative board is responsible for appointing and generally dismissing the members of the management board or the managing directors. The maximum term of office is five years in an AG and six years in an SE; a reappointment or extension is principally permitted.

The members of the supervisory and administrative board are appointed by the general meeting, for a maximum term of office of approximately five years in an AG and six years in an SE. Reappointment is permitted. Dismissal could happen by resolution of the general meeting with a majority of at least three quarters of the votes cast, unless the articles of association provide otherwise. Employee representatives on the

supervisory board in the case of codetermination are generally appointed by employee elections.

The appointment and dismissal of the managing directors of a GmbH is, in principle, the responsibility of the shareholders' meeting. The term of office may be indefinite.

A person who has been convicted of certain criminal offences (eg, fraud) may not be a member of a management board nor a managing director.

4.5 Rules/Requirements Concerning Independence of Directors Management Board

The members of the management board of an AG are subject to a duty of loyalty to the company, must observe the best interests of the company, and are bound by a non-compete obligation for the duration of office. They must disclose conflicts of interest to the supervisory board without undue delay. The DCGK also makes statements to that effect. In certain situations, members of the management board should thus either abstain from casting votes or not even participate in the meeting or the relevant topic.

Supervisory Board

The members of the supervisory board of an AG and a two-tier system SE and of the administrative board of a single-tier system SE are also bound by a duty of loyalty, but there are no mandatory statutory provisions that require and define independence. However, a few restrictions aiming at independence prohibit an individual from becoming a member of the supervisory or administrative board – eg, where the individual is part of the management of a subsidiary of the company. Nevertheless, the DCGK requires

a certain degree of independence to avoid conflicts of interest.

In this respect, the supervisory board shall determine an appropriate number of independent members. The DCGK gives indicators for determining the independence of members of the supervisory board. These include personal or business relationships with the company, the management board, controlling shareholders and major competitors that may cause a substantial or not merely temporary conflict of interest.

4.6 Legal Duties of Directors/Officers

Members of management bodies must conduct the company's affairs with the due care of a prudent and diligent businessman, in particular in accordance with the applicable laws and the articles of association (duty of legality, including and of ever-increasing importance the duty to establish and maintain an effective compliance management system). In the case of entrepreneurial decisions, the so-called business judgment rule applies in order to eliminate hindsight bias when legally evaluating the management bodies' past conduct. This means that members of the management board may be exempt from liability if they had reasonably assumed that they were acting on the basis of adequate information and in the best interests of the company.

The same applies to the members of the supervisory and administrative board. However, their differing tasks and roles in the corporate governance of the respective company lead to a different emphasis of duties.

4.7 Responsibility/Accountability of Directors

In principle, members of management and supervising bodies owe their duties primarily to

the company; they always have to act in the best interests of the company and its group. However, the interests of the company include, to a certain extent, the interests of all stakeholders (such as creditors and employees) of the company (the German “*stakeholder model*” in contrast to the Anglo-Saxon “*shareholder model*”).

4.8 Consequences and Enforcement of Breach of Directors’ Duties

In an AG and SE (with a few exceptions in special statutory rules – eg, in the event of an insolvency or in the context of wilful misconduct), creditors and shareholders cannot enforce a breach of duties of members of management and supervising bodies. The members of the bodies are rather jointly and severally liable in the internal relationship towards the company due to their joint responsibility. Thus, individual members of a management and supervising body may not absolve themselves from liability because a certain task or responsibility was delegated to a different member internally.

Furthermore, such a breach may lead to a dismissal and, with respect to the management members, a termination of their service contract.

In principle, the supervisory board is responsible and – according to case law – even has a duty to assert damage claims to the management board members. The company may waive its damage claims or enter into settlement arrangements on these claims only if three years have lapsed since the claim arose and the general meeting resolved thereupon without a minority of the shareholders (at least 10% of the share capital) raising an objection.

Where members of the supervisory board culpably breach their duties, the management board is responsible for pursuing possible damage

claims against the supervisory board members jointly and severally.

Claims Against Members of Corporate Governance

The rights and obligations on asserting claims against members of corporate governance bodies in an AG, SE and KGaA are independent of whether or not the members of these respective bodies have been discharged. Another particular consequence of a breach of duty in a listed company is that the company may be obliged to disclose it to the capital market by way of ad hoc notification.

In the case of a GmbH, the consequences of a breach of the duties of managing directors are, to a great extent, comparable to an AG. In general, the managing directors, like the management board members, are not directly liable to the creditors of the company. The shareholders’ meeting has the right to pursue damage claims and to decide about the dismissal of managing directors and the termination of the service contract.

In contrast to the situation in the AG, if the shareholders’ meeting has discharged the managing director knowing the facts underlying such a breach, the discharge leads to an exclusion of liability.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Certain special law remedies and, in the case of wilful misconduct, general civil law remedies, exist. From the company’s point of view, these do not generally extend claims any further than those under corporate law. Since shareholders do not have a direct claim against the members of management and supervising bodies under corporate law, in certain situations (eg, capital

market fraud) general civil law remedies may provide an opportunity for claims of shareholders.

However, the courts have traditionally been cautious in recognising such claims.

Liability

The liability of a member of a management and supervising body in an AG, SE and KGaA cannot be limited, as this would in particular qualify as an impermissible waiver by the company upfront – ie, prior to the expiry of the three-year period (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**). However, D&O insurance for the members of the management and supervising body is permissible and common in practice in order to protect them against risks arising from their professional activities for the company. Premiums are generally paid by the company, although members of the management board of an AG, SE and KGaA are obliged to bear a deduction of at least 10% of the damage to one-and-a-half times their annual fixed salary at maximum.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Remuneration of the Management Board

The remuneration of the management board members of an AG and a two-tier system SE is resolved by the supervisory board and contractually agreed upon in the service contract.

In listed companies, the supervisory board has to determine the principles of the remuneration of the members of the management board in a remuneration system, which is subject to approval by the general meeting upon its introduction and any material changes thereto, at least every four years. However, the resolution

on the approval is non-binding and thus has no effect on the legitimacy of the remuneration. Nevertheless, if the general meeting does not approve the remuneration system, a reviewed remuneration system has to be presented at the next annual general meeting for approval.

Contents

With respect to the contents of the remuneration system, the AktG only requires a few elements to be included in every remuneration system (eg, a maximum total remuneration of the management board) but provides for further rules with respect to its contents relating to different aspects of the remuneration of the management board if those aspects are foreseen in the remuneration system. However, the DCGK makes several recommendations with respect to criteria to be described in the remuneration system – eg, the ratio between the fixed remuneration and the variable remuneration based on short- and long-term incentives, as well as the performance and non-performance indicators for determining payment of variable remuneration.

The supervisory board then determines the actual remuneration of each member of the management board based on the remuneration system. The supervisory board and the management board have to prepare a remuneration report regarding the past financial year, which is subject to a non-binding approval by the annual general meeting. Neither the resolution on the remuneration system nor the resolution on the remuneration report can be objected to by means of a contesting action or an action for annulment by a shareholder.

Restrictions

As regards restrictions on the remuneration of the members of the management board, the AktG requires that the overall remuneration of

individual members of the management board is appropriate in relation to their tasks and performance as well as the economic situation of the company. In addition, the supervisory board must ensure the customary remuneration is not exceeded. Further, the remuneration in listed companies has to be aimed at a sustainable and long-term-oriented development of the company, and variable remuneration should be granted based on long-term incentives accordingly.

If the supervisory board culpably disregards the statutory requirements when determining the remuneration for the management board, it may be held liable for damages.

Characteristics

The DCGK makes further recommendations with respect to the characteristics of the remuneration. For example, it recommends that the variable remuneration based on long-term incentives exceeds the one based on short-term incentives. Variable remuneration shall be predominantly invested in shares of the company or granted as share-based remuneration.

The DCGK further recommends that payments to members of the management board due to early termination of their activity do not exceed twice the annual remuneration (severance cap) and do not constitute remuneration for more than the remaining term of the contract. Another suggestion is that change-of-control clauses should not be agreed upon.

Supervisory Board

The remuneration of the supervisory board members may be specified in the articles of association or granted by the general meeting. It should be appropriate in relation to the tasks of the members of the supervisory board and the company's economic situation. In listed compa-

nies, the general meeting has to resolve on the remuneration of the supervisory board members at least every four years, also in a non-binding manner, with the resolution including or referencing the same details that are to be included in the remuneration system of the management board with respect to the remuneration of the supervisory board members, if applicable. The DCGK further recommends taking into consideration the status as chair or deputy chair of the supervisory board or committee in this context. It is suggested that the supervisory board remuneration be a fixed remuneration.

Managing Directors and General Partners

In a GmbH, the remuneration of managing directors is the responsibility of the shareholders' meeting, which must not adhere to any restricting rules.

In a KGaA, the general partners generally receive no remuneration for their activities, but are entitled to receive a fee for taking over the liability of the KGaA vis-à-vis third parties. In the case of a capital company as general partner, the remuneration of its management members is to be set according to the rules applying to the respective legal form of such a capital company.

4.11 Disclosure of Payments to Directors/Officers

All capital companies are required to disclose the total remuneration of the management board in the annual financial statements. An exception is made only for capital companies that fulfil at least two of the following criteria (small capital companies):

- the balance sheet total does not exceed EUR7,5 million;
- the sales revenues within the last 12 months amount to less than EUR15 million; and

- the company employs, on an annual average, fewer than 50 employees.

In a listed company, the features of the remuneration system must be described (see **4.10 Approvals and Restrictions Concerning Payments to Directors/Officers**). The remuneration system has to be published on the company's website for the duration of the application of the remuneration system – however, at least for ten years. In addition, the management board and the supervisory board of a listed company must disclose certain information, such as the fixed and variable remuneration paid to each member of the management and the supervisory board, in the annual remuneration report. The remuneration report is also published on the company's website for at least ten years. The AktG requires the remuneration report to be audited.

The AktG also requires ad hoc and annual disclosure of related party transactions, including transactions of the company with its various members of corporate bodies.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The purpose of the company is determined by its shareholders in the articles of association. The shareholders can only exert influence on the decision-making process by way of resolutions. The general meeting of an AG, SE and KGaA has fewer rights and powers than the shareholders' meeting of a GmbH, in particular due to their ability to instruct the managing directors (see **3.2 Decisions Made by Particular Bodies**).

Furthermore, the shareholders have fiduciary duties towards the company and the other

shareholders, and so have to promote the purpose of the company and may not act to its detriment.

5.2 Role of Shareholders in Company Management

The involvement of the shareholders in the management of a company differentiates according to the legal form of the company.

AGs, SEs and KGaAs

In an AG, SE and KGaA, the general meeting is entitled to appoint the members of the supervisory and administrative board, generally by simple majority, and to dismiss them by 75% of the share capital represented. However, the members of the management board and the managing directors in a single-tier system SE are appointed by the supervisory board, respectively the administrative board. The general meeting cannot instruct the supervisory or administrative board, or the management board.

If the management board so requires, the general meeting is entitled to resolve upon management affairs. In practice, such requests do not happen often. Apart from this, the general meeting does not have any influence on the management.

Listed Companies

Listed companies also do not engage with their shareholders, in particular not outside the general meetings. In preparing such meetings, the CEO has calls with shareholder representatives and potential proxy voters, but abstains from providing them with any information that has not already been disclosed in the invitation or that the CEO does not intend to disclose in the general meeting to all other shareholders. However, the DCGK suggests that the chairman of the supervisory board should, to an appropriate

extent, be in regular conversation with investors on supervisory board-related issues.

Non-listed Companies

Conversely, non-listed companies typically do engage with their shareholders.

GmbH

In a GmbH, the involvement of the shareholders in the management is also statutorily more extensive. In contrast to the AG, the shareholders' meeting resolves upon the appointment and dismissal of the managing directors and on the conclusion of their service agreements. Also, the shareholders of the GmbH are able to direct the managing directors to take or refrain from taking certain actions in the business by way of internally binding instruction.

5.3 Shareholder Meetings

Annual General Meetings

An annual general meeting is mandatory in an AG and KGaA within the first eight months of a financial year, and in an SE within the first six months of a financial year. The annual meeting has to resolve upon the ordinary topics (see **3.2 Decisions Made by Particular Bodies**) and upon the remuneration system, the latter resolution being non-binding (see **4.10 Approvals and Restrictions Concerning Payments to Directors/Officers**). Further extraordinary topics on fundamental decisions can also be put on the agenda of the annual general meeting, or can be passed in an extraordinary general meeting.

Apart from this, general meetings are to be convened if necessary for the welfare and going concern of the company. The general meeting has to be convened no later than 30 days prior to the date of the general meeting, or no later than 36 days prior to the meeting if shareholders are required to register for the general meeting. In

an AG and a two-tier system SE, the convening is generally the obligation of the management board, or exceptionally the supervisory board. Within a single-tier system SE, the administrative board is responsible for the convening.

However, shareholders whose share is equivalent to at least 5% of the registered share capital may also demand the convening of a general meeting. Shareholders whose share in the share capital is that high or corresponds to a nominal stake of EUR500,000 may demand that certain additional items are put on the agenda. The demand has to be received by the company 24 days prior to the general meeting at the latest, or no later than 30 days prior to the general meeting for listed companies.

Virtual General Meetings

In August 2022, the German Parliament passed a new law introducing virtual general meetings – ie, meetings without the physical presence of the shareholders or their proxies at the location of the general meeting, as a permanent option and alternative to the physical general meeting. However, pursuant to the new provisions, virtual general meetings require a corresponding provision or authorisation in the articles of association as of 31 August 2023. Such provision or authorisation may only be set for a maximum term of five years.

Annual General Meeting Invitation

The invitation has to fulfil a lot of formalities, such as setting out the business name and seat of the company, the time and place of the general meeting, and the agenda. For listed companies, the invitation has to provide further information – eg, about the rights of the shareholders in respect of the general meeting.

Votes and Resolutions

Unless stipulated otherwise in the articles of association, the general meeting should be held at the seat of the company. Resolutions may not be taken by written consent, but the articles may provide that shareholders can cast votes in written form. Shareholders may be represented by a proxy/proxy voter at the general meeting, or may exercise their rights via electronic communication; the latter option is only available if the articles of association allow this form of attendance and voting.

In listed companies, each resolution adopted by the general meeting is to be recorded in the minutes of the meeting prepared by a notary public. For non-listed companies, it is sufficient to have the minutes signed by the chairman of the supervisory board as long as no resolutions are adopted for which applicable law requires a majority of 75% of the votes cast or a greater majority.

GmbHs

In a GmbH, the regulations in respect of the shareholders' meeting are not as strict as in the AktG for AGs, SEs and KGaAs. Resolutions generally have to be passed in a meeting of the shareholders, but can also be made in writing based on a corresponding provision in the articles of association or provided that all shareholders agree in text form. The shareholders' meeting generally has to be convened by the managing directors by registered letter.

In the case of a meeting, the invitation must be sent at least one week before the meeting, and the agenda of the shareholders' meeting has to be announced in the invitation. However, these formalities on the invitation can be waived or amended in the articles of association.

There are no special requirements for the holding and conducting of shareholders' meetings. Shareholders may submit their vote in writing or may grant proxy. It is also permissible to hold virtual meetings via electronic communication based on a corresponding provision in the articles of association or provided that all shareholders agree in text form.

5.4 Shareholder Claims

Shareholders generally do not have any direct claims against members of corporate governance bodies (see 4.8 Consequences and Enforcement of Breach of Directors' Duties and 4.9 Other Bases for Claims/Enforcement Against Directors/Officers).

Appealing Resolutions

Any shareholder who holds only "one" share may appeal resolutions (*Anfechtungs- und Nichtigkeitsklage*) of the general or shareholders' meeting for breach of law or the company's articles of association. Another objection shareholders can try to bring forward in such lawsuits is the violation of the (majority) shareholder's duty of good faith. As these duties are not statutorily defined, the chances of success are based on case law. The defendant is the company, not the other shareholder/shareholders who has/have voted in favour.

By filing such objection and avoidance claims in court, minority shareholders can block the completion (ie, entry into the commercial register) of, for example, corporate and integration measures. Registration will take place when the minority shareholders' court challenges are overcome by a so-called release proceeding, which the company must file (*Freigabeverfahren*). The company will particularly prevail in the release proceeding and thereby achieve registration in the commercial register if minority shareholders

cannot prove that they hold more than a nominal value of EUR1,000 of the registered share capital of the company since the announcement of the convocation of the general meeting.

If in the context of a resolution the company or a majority shareholder has to offer to acquire shares of minority shareholders at fair value based on an IDW S1 valuation, those resolutions cannot be objected to (any more) with the argument that the valuation is too low. However, minority shareholders are entitled to challenge the adequacy of the price in court in a special shareholder compensation proceeding (*Spruchverfahren*).

Appointing a Special Auditor

Shareholders can request (by demanding either an invitation of an extraordinary general meeting or the adding of a topic on the agenda, see 5.2 Role of Shareholders in Company Management) that the general meeting shall – with a simple majority of the votes cast – appoint a special auditor (*Sonderprüfer*) to analyse statutorily specified decisions of the executive and supervisory board. If the general meeting rejects the motion to appoint a special auditor, and if facts and circumstances justify severe breaches of tasks and duties by the management, minority shareholders who together hold 1% of the registered share capital or a nominal value of at least EUR100,000 can file for the appointment of the special auditor in court.

Damage Claims

Minority shareholders may influence the assertion of damage claims against management and supervisory board members following breaches of tasks and duties if, in a first instance, the general meeting resolves with a simple majority to assert such claims. Minority shareholders who together hold 10% of the registered capi-

tal or a nominal value of at least EUR1 million can then judicially file for the appointment of a special representative (*besonderer Vertreter*) to assert these claims. Minority shareholders who together hold 1% of the registered share capital or a nominal value of EUR100,000 or more can also apply in court for admission to assert these claims of the company in their own name.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Shareholders of listed companies have to notify the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* or BaFin) and the issuer if their direct and/or indirect holdings exceed or fall below certain thresholds (3%, 5%, 10%, 15%, 20%, 25%, 30%, 50%, 75%) and if their positions in financial instruments relating to shares exceed or fall below the aforementioned thresholds (except for the 3% threshold). The notification is to be published by the issuer and can be viewed on its website at any time. Shareholders of listed companies who directly or indirectly hold at least 10% must notify the issuer of the objectives pursued with the acquisition and the origin of the funds used within 20 trading days of reaching or exceeding this threshold.

According to the Money Laundering Act (*Geldwäschegesetz*, GWG), which implements the EU Anti-Money Laundering Directive, companies need to disclose their beneficial owner(s) in the transparency register, irrespective of whether their shares are publicly traded or not.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Except for small partnerships, companies have to prepare an annual financial statement. Capital companies additionally have to prepare a management report, unless the company is a small company (based on the criteria set out in **4.11 Disclosure of Payments to Directors/Officers**). The annual financial statements and the management report differ in that the annual financial statements are primarily for presentation purposes, whereas the management report is more of an analysis and commentary.

The management report includes information on the risk profile of the company and its risk management system. For large, listed companies, the HGB requires a declaration on corporate governance and a non-financial declaration including statements on environmental, social and labour-related concerns, among other matters.

In addition to preparing the annual financial statements and the management report, listed companies are also required to prepare and publish a half-year report. Some stock exchanges may require further reporting with respect to a certain market segment.

Certain industry sectors – for example, banks and other financial institutions – are subject to further reporting requirements.

6.2 Disclosure of Corporate Governance Arrangements

The declaration on corporate governance includes information on how the management board and the supervisory board conducted their duties, and also has to address other issues,

such as whether quotas for female members of the management and supervisory board have been met, and whether or not the company has a diversity concept (see **4.3 Board Composition Requirements/Recommendations**). Furthermore, listed companies have to publicly declare each year whether they comply with the DCGK (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**). The declaration is part of the declaration on corporate governance and must be published on the website.

As described, the remuneration system as well as the remuneration report must be published on the company's website for at least ten years. Further, the principal features of the management remuneration system and the remuneration of the management board and the supervisory board must be disclosed in the annual financial statement and in the management report thereto.

The annual financial statement also has to include information on related party transactions that were not at arm's length. Certain related party transactions must also be disclosed on an ad hoc basis.

6.3 Companies Registry Filings

A company must in particular file the following with the commercial register (*Handelsregister*):

- the articles of association, including the company's business name and legal form, registered seat, purpose of the enterprise and registered share capital;
- the names of the legal representatives, their place of residence and dates of birth;
- if existent, the name and place of residence of authorised officers (*Prokurist*);

- in an AG and SE, a list of supervisory and administrative board members;
- in a GmbH, a list of shareholders; and
- subsequent amendments to the above-mentioned points.

Those filings are publicly available at www.han-delsregister.de, which contains all entries in the commercial register filed since 2007.

The entry in the commercial register is constitutive in certain cases (eg, foundation, mergers or changes of legal form of the company), which means the measure will only become effective upon its entry in the commercial register. In other cases, failures to make filings may result in a fine from the registry court.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

A company has to appoint an external auditor unless it is a small company (based on the criteria set out in **4.11 Disclosure of Payments to Directors/Officers**). The key requirements governing the relationship between the company and the auditor are set out in the HGB. The auditor is appointed by the general or shareholders' meeting. In an AG and two-tier system SE, the supervisory board is responsible for issuing the actual audit mandate; while in a single-tier system SE it is the administrative board, and in a GmbH it is the managing directors.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

In an AG, SE and a KGaA, the management board must install a system to detect and monitor risks to the continued existence of the company. However, it is best practice to maintain several systems and refined rules (for example, through reporting lines and codes of conduct) to ensure internal compliance and effective risk management. Specifically, the management board of a listed company is required by law to establish an internal control and risk management system. The supervisory board will review the existence and effectiveness of such measures. Managing directors of a GmbH are also expressly obliged to take measures for the early detection of a crisis.

According to German case law, effective compliance management systems are also required in order to fulfil the duty of care owed to the company.

Trends and Developments

Contributed by:

Stephan Waldhausen, Moritz Pellmann, Justus Anacker and Cristina Hajek Gross
Freshfields

Freshfields has a corporate governance practice defined by its international reach and its ability to provide consistent expert advice on all aspects of corporate governance law across Europe's major jurisdictions. In Germany, the practice advises public and private companies, as well as supervisory and management boards, on a broad range of governance matters, including board responsibilities, regulatory compliance and the structuring of governance frameworks. It is regularly involved in significant corporate events such as mergers, strategic transactions, leadership changes, in-

ternal investigations, and crisis response. With extensive cross-border experience, the practice supports clients in navigating governance issues across jurisdictions, ensuring consistency with both German and international legal standards. It also advises on shareholder engagement, activism-related matters, and disclosure obligations. The practice's work is grounded in legal and regulatory analysis, with a focus on enabling sound governance structures and informed decision-making in complex and evolving regulatory environments.

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GERMANY TRENDS AND DEVELOPMENTS

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FRESHFIELDS

Navigating the Complex Future of German Corporate Governance in 2025: Strategic, Regulatory and Ethical Challenges

In 2025, corporate governance in Germany is being reshaped by a combination of regulatory, geopolitical and technological disruptions. At the same time, scrutiny of business judgement decisions is increasing. For boards, this requires strategic foresight, adaptability, scenario planning and robust oversight:

- **Legal and strategic uncertainty:** Regulatory volatility and geopolitical instability are making long-term planning a minefield. Sustainability standards are shifting rapidly, with once-accepted norms facing increasing scrutiny amid polarised climate policy debates. Global conflicts and shifting alliances are altering trade flows, with sanctions imposed or lifted and new economic blocs emerging. This dynamic environment challenges strategic clarity that boards must maintain amid the growing complexity.
- **Artificial intelligence disruption:** Artificial intelligence (AI) is transforming business models – from automating operations to enabling predictive strategies. But with innovation comes risk: regulatory grey zones, ethical dilemmas, and workforce transformations. Boards must strike a balance between embracing AI and ensuring responsible governance.
- **Data and cybersecurity risks:** Cyber threats are more sophisticated than ever. Data is both an asset and a risk. Boards must treat cybersecurity not as an IT issue, but as a central governance priority – failure to do so risks severe operational and reputational harm.
- **Complex business judgements:** The rate of business failure is increasing due to inadequate due diligence, poor risk management and poor decision-making. In an increasingly risk-prone and complex business environ-

ment, such failings can have far-reaching consequences. To avoid personal liability, board members must comply with the Business Judgement Rule (BJR). This means that they must base their business decisions on adequate information, avoid or deal with conflicts of interests and act in the best interests of the company. Boards that fail to meet this standard risk not only legal exposure, but also a loss of stakeholder trust.

The year 2025 will test the resilience and adaptability of executive leadership. With Germany at the centre of global regulatory and technological shifts, boards must be equipped with the insight and agility to navigate a highly complex and unpredictable landscape.

Legal and Strategic Uncertainty

Increasingly diverging regulatory requirements, shifting societal norms, and geopolitical volatility are creating a landscape of legal and strategic uncertainty. Boards must navigate polarised sustainability debates and evolving geopolitical alliances with heightened caution and clarity.

Sustainability

The sustainability agenda is increasingly fragmented. While some advocate climate-first policies, others question the economic impact of heavy regulation. In Germany, corporate sustainability efforts face criticism for being overly bureaucratic and costly.

Supply chain regulation

Germany's Supply Chain Act (*Lieferkettensorgfaltspflichtengesetz*, LkSG), in force since 1 January 2023, was initially welcomed as a milestone in promoting human rights and environmental standards in global supply chains. However, it has since faced criticism, particularly from the business community, for being overly complex

and burdensome, affecting around 5,000 companies. In response, the newly elected German government has announced plans to repeal the Act and align with the EU-wide Corporate Sustainability Due Diligence Directive (CSDDD, (EU) 2024/1760).

While the CSDDD shares similar objectives and due diligence obligations, it includes a civil liability clause, increasing legal exposure for companies. However, after the EU Commission released the “Omnibus” packages on 26 February 2025, the CSDDD is likewise facing regulatory amendments. The Omnibus packages are the EU Commission’s proposals to simplify EU rules, reduce administrative burdens, and enhance competitiveness. Through these legislative initiatives, the EU Commission seeks to create a more favourable environment for trade and investments across the EU.

Following the Omnibus packages, the CSDDD is currently under revision. The proposed amendments include:

- limiting due diligence to direct suppliers rather than the entire supply chain;
- reducing obligations and thus administrative load for small and medium sized enterprises (SMEs);
- relaxing climate plan requirements;
- permitting longer intervals between compliance audits; and
- removing the standardised civil liability provision.

The new German government has expressed a strong commitment to adopting the Omnibus legislative packages. It aims to streamline national procedures by eliminating the requirement to report to the Federal Office for Economic Affairs and Export Control (BAFA) and

by reducing associated sanctions. At the same time, it intends to uphold essential due diligence obligations – such as the requirement to regularly assess human rights and environmental risks within the company’s own operations and those of its direct suppliers – until the Corporate Sustainability Due Diligence Directive (CSDDD) is fully implemented.

At the initiative of the Omnibus packages, the newly adopted Stop-the-Clock Directive ((EU) 2025/794) extends the transposition deadline of the CSDDD to 26 July 2027, with the first application phase for the largest companies deferred to 26 July 2028 (initially, EU Member States were required to adopt the CSDDD by 26 July 2026, with phased requirements beginning in 2027). This extension provides legislators with additional time to finalise substantive amendments to the CSDDD, including simplifying due diligence requirements.

For now, companies must remain compliant with existing requirements in Germany while preparing to transition to the simplified EU framework. Close monitoring of regulatory developments will be essential to leverage reduced reporting and compliance burdens as they take effect.

Sustainability reporting

Sustainability reporting has transitioned from a voluntary initiative to an increasingly expected practice aimed at fostering corporate accountability and supporting risk management. However, as it becomes more widespread, so does the risk of greenwashing, where companies may present an exaggerated or misleading picture of their environmental and social performance. Amid this shifting environment, debates around the effectiveness and burden of sustainability reporting continue to intensify.

Germany has not yet transposed the Directive (EU) 2022/2464 on Corporate Sustainability Reporting (CSRD) into national law, missing the July 2024 deadline. As a result, the EU Commission launched infringement proceedings against Germany (and 16 other EU Member States) in September 2024. The CSRD requires large and listed companies to report in line with the EU Sustainability Reporting Standards (ESRS; Commission Delegated Regulation (EU) 2023/2772), which establish binding, harmonised standards to ensure the comparability of sustainability information across the EU. However, German implementation of the CSRD stalled ahead of the February 2025 federal elections and now awaits action from the new German Bundestag.

In February 2025, the EU Commission proposed narrowing the CSRD's scope in response to concerns over excessive bureaucracy. Under their revised proposal, only companies meeting the following thresholds would be subject to the directive:

- more than 1,000 employees;
- either over EUR50 million in turnover or EUR25 million in total assets.

This would exempt around 80% of previously affected companies.

Similarly, under the EU Commission's proposal, Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment (EU Taxonomy Regulation) will apply only to companies with:

- at least 1,000 employees;
- EUR450 million in global turnover.

Meanwhile, the already enacted Stop-the-Clock Directive grants a two-year delay for companies

originally scheduled to report in 2026 or 2027 (so-called Wave 2 and 3 companies), allowing time for EU co-legislators to finalise the proposed amendments in the Omnibus packages. However, large public interest entities with more than 500 employees (so-called Wave 1 companies), are still expected to report under the CSRD in 2025 for the 2024 financial year.

In the absence of national implementation of the CSRD, companies in Germany must still comply with sustainability reporting requirements set out in the German Commercial Code (*Handelsgesetzbuch*, HGB). This includes submitting a non-financial statement as part of the management report for large publicly traded companies with more than 500 employees.

Whether reporting in 2026 (covering the 2025 financial year, for Wave 1 companies) will be governed by the CSRD depends on the pending transposition law. Until then, it is uncertain whether the CSRD will apply to 2026 reporting in Germany.

In the meantime, companies may voluntarily apply the EU Sustainability Reporting Standards (ESRS) under the HGB. According to the guidance of the Institute of Public Auditors in Germany (*Institut der Wirtschaftsprüfer in Deutschland*, IDW), companies may adopt the ESRS in their non-financial statements to the extent they want – in full, in part, or not at all.

Voluntary adoption can enhance transparency and build stakeholder trust, while also preparing companies for future regulatory requirements. However, it carries risks such as increased scrutiny and potential accusations of greenwashing. Companies must carefully weigh these factors. Despite the challenges, many German firms are already choosing to align with the ESRS frame-

work, at least partially, as part of their sustainability reporting strategy.

Geopolitical risks

Geopolitical tensions continue to reshape global trade and investment. German companies must anticipate disruptions to supply chains, market access, and competitive positioning. Boards should prioritise resilience and risk management strategies to adapt to these external pressures.

Since 2022, the EU has steadily expanded sanctions against Russia. The Council Regulation (EU) 2025/392 of 24 February 2025, amending Regulation (EC) No 765/2006, introduced the 16th sanctions package, including an import ban on Russian aluminium and tighter dual-use export controls. On 14 May 2025, the EU reached political agreement on a 17th package targeting Russia's so-called "*shadow fleet*", expanding export bans, and adding new designations. The package was formally adopted on 20 May 2025, at which point the UK also announced further, wide-ranging sanctions. At the same time, the EU confirmed that a 18th package was already being prepared, with the aim of preventing the reactivation of the Nord Stream gas pipelines, lowering the price cap on Russian oil and further targeting Russia's financial sector.

In parallel, Directive (EU) 2024/1226 requires EU Member States to criminalise: (i) intentional breaches of sanctions; (ii) the circumvention of asset freezes or restrictions on financial services; and (iii) serious negligence in relation to trade restrictions. Adopted on 24 April 2024, the directive requires transposition into national law by 20 May 2025. Legal entities will be held accountable for violations by personnel in leading positions, whether acting alone or as part of an organisational body.

Germany must adapt its regulations to comply with Directive (EU) 2024/1226. Violations of sanctions are governed by the Foreign Trade and Payments Act (*Außenwirtschaftsgesetz*, AWG) and the Foreign Trade and Payments Ordinance (*Außenwirtschaftsverordnung*, AWV). Although the former German government proposed amendments, its newly elected successor plans to draft its own, likely making previous efforts obsolete. In alignment with this shift, the new government has expressed strong support for the EU's initiative to strengthen sanctions against Russia. Consequently, companies should focus on developing "*asset light*" models to minimise exposure in geopolitically risky regions and plan strategic exit options like negotiating put options into contracts or partial sales.

To mitigate geopolitical risks, boards should:

- diversify supply chains;
- strategically review and adapt international contracts;
- conduct scenario planning and "*What if?*" analyses;
- develop contingency and exit strategies.

Boards should also enhance reporting on geopolitical risks to meet the expectations of investors, regulators, and business partners. Leveraging internal and external geopolitical expertise will be key to informed decision-making.

AI Disruption

The integration of AI into corporate operations and decision-making marks a structural shift in governance, comparable in scale to the Industrial Revolution but advancing at a significantly faster pace. From predictive analytics to generative models, AI is transforming how companies operate, compete and strategise. It enables operational efficiency, personalised engagement

and enhanced market foresight. Generative AI, in particular, accelerates innovation by automating knowledge-intensive tasks.

However, this massive potential introduces new uncertainties. Rapid AI development challenges business models, disrupts sectors, and raises complex ethical and legal questions. For boards, the task is not merely adoption, but responsible governance aligned with fiduciary duties.

Therefore, boards should institutionalise the following six key principles with respect to the usage of AI generated information in decision-making processes at board level:

Legality

The board must ensure compliance with all applicable laws, particularly AI-specific regulations such as the EU AI Act and data protection regulation such as the GDPR (Regulation (EU) 2016/679).

Careful decision-making

Boards must make well-informed decisions on whether and how to deploy AI, weighing both opportunities and risks. Given the potential impact of AI developments on most businesses, abstaining from decision-making is no longer a risk-free option. Consequently, the management and supervisory boards should establish clear responsibilities through their internal rules of procedure.

Non-delegable responsibility

While AI can support decision-making, the ultimate responsibility and decision-making authority must remain with human board members. Furthermore, board members must validate the AI's output and assess its plausibility. The rationale behind AI-generated recommendations must be both explainable and traceable. The board must

also be able to demonstrate how AI-informed decisions were reached, and explain why these decisions were reasonable and in the company's best interests.

Human supervision

The board members need to ensure continuous supervision of AI systems, especially for those that learn and evolve, to identify potential malfunctions or unintended outcomes.

Technical competence

Board members also need to ensure that the organisation has sufficient knowledge of AI use, since understanding, overseeing and critically assessing AI-generated results is essential.

Organisational measures

If AI tools are introduced, boards are expected to implement effective risk management, monitoring, and documentation processes for AI usage. This includes:

- regular audits of AI systems to detect and correct bias in training data and outputs, in order to reduce the risk of discriminatory outcomes and support the legitimacy of AI-assisted decisions;
- protection of AI systems against manipulation, external attacks, and operational failures (including aligning with recognised cybersecurity standards and ensuring resilience when integrating AI into existing IT infrastructures);
- continuous monitoring and documentation of the performance, stability, and data quality of AI systems, ensuring that AI systems remain fit for purpose.

The EU's AI Act (Regulation (EU) 2024/1689) reinforces these requirements by introducing a binding classification system for AI applications, including prohibited risk (eg, social scor-

ing), high-risk, limited and minimal risk systems. High-risk systems, which are common in enterprise environments, are subject to stringent obligations concerning transparency, data governance, and human oversight. Limited-risk systems must meet standards for explainability and user awareness, while minimal risk systems are largely exempt from regulatory obligations. The board must ensure that the applicable regulatory obligations are embedded into the organisation's governance architecture and are complied with.

Data and Cybersecurity Risks

In the digital economy, data serves as both a strategic asset and a critical point of vulnerability. As digital integration deepens, cybersecurity has become a top governance priority for companies. Increased interconnectivity exposes firms to threats such as data breaches, ransomware, industrial espionage, and hybrid attacks on critical infrastructure.

Cyber threats surged in 2024, with Distributed Denial of Service (DDoS) attacks on European businesses – designed to overload systems with excessive traffic, disrupting normal operations – more than doubling. In Germany, 9% of companies reported incidents of industrial espionage, most involving sophisticated hacker activity. Reflecting the growing urgency, the President of BaFin (*Bundesanstalt für Finanzdienstleistungsaufsicht*), Germany's Federal Financial Supervisory Authority, issued a public warning in January 2025, highlighting the escalating cyber risk facing financial institutions and insurers.

The EU has implemented an enhanced regulatory framework in response. Directive (EU) 2022/2555 on measures for a high common level of cybersecurity across the Union (NIS2 Directive) expands obligations across 18 critical sectors, introducing stricter reporting duties and

direct board accountability. Germany has yet to transpose the NIS2 Directive, after the February 2025 elections prevented the passing of a proposed draft implementation act.

In parallel, Regulation (EU) 2022/2554 on digital operational resilience for the financial sector (Digital Operational Resilience Act; DORA) entered into force on 17 January 2025. It imposes binding cybersecurity and resilience requirements on financial entities and information and communication technology (ICT) providers. Together with the GDPR, the NIS2 Directive and the DORA form the EU's digital risk governance regime.

Cybersecurity is no longer a solely technical issue. Under the German Stock Corporation Act (*Aktiengesetz*, AktG), the board is legally obliged to implement systems that detect and mitigate security risks, including cyber threats. The board, therefore, needs to implement governance structures suited to a digitalised environment. Boards should ensure that they:

- enhance IT literacy among their members to ensure informed oversight of digital risks;
- integrate redundancy and backup protocols to maintain operational continuity;
- implement and test incident response plans to ensure preparedness;
- foster co-ordination between IT, legal, compliance, and risk functions for a unified response.

Cybersecurity must be a standing agenda item for boards, with regular updates, sustained investment, and clear accountability. Inaction risks serious legal, financial, and reputational consequences. And, again, boards must establish clear responsibilities for both management and supervisory levels.

Complex Business Judgements

The accelerating complexity of global markets, regulatory frameworks, and technological disruption has elevated the stakes of board-level decision-making. Strategic decisions are increasingly made in contexts where information is incomplete, risks are multilayered and interdependent, and outcomes are difficult to predict.

However, complexity does not absolve responsibility. On the contrary, it demands a more structured and disciplined decision-making approach. In such an environment, inadequate board judgement can quickly escalate into personal and corporate liability. Over the past decade, there has been a significant increase in cases where not only compliance incidents but also business judgements made by boards have been retrospectively investigated if they resulted in (significant) losses. Additionally, the expectations for engagement and supervision by supervisory boards have risen, effectively tightening the duties of their members. Consequently, it is increasingly important for board members to focus on meeting the requirements of the Business Judgement Rule (BJR). Failure to do so shifts the burden of proof to the board members, requiring them to demonstrate that they were acting in alignment with their duties. Meeting the BJR requirements safeguards board members from liability. This requires that decisions are made (i) on the basis of adequate information; (ii) in the best interest of the company; and (iii) in good faith and without conflicts of interests.

To meet this standard, boards should embed the following questions in their decision-making processes:

- To the extent AI-generated information is used in the decision-making process, have we complied with the six key principles regarding AI usage set out above?
 - Have underlying assumptions been critically reviewed and checked for plausibility?
 - Is external (independent) professional advice required to ensure the adequacy of the information basis or to provide guidance on an unclear legal framework?
 - Have all relevant business opportunities (including alternative scenarios) and risks for each of the relevant decision options been adequately assessed and balanced against each other?
 - Are board members subject to potential conflicts of interest?
 - Are we aware of the burden of proof and, if so, is there a proper documentation process in place, laying out that the BJR requirements are met (also taking into account the aspects mentioned in the aforementioned bullets)?
- In a high-stakes environment, governance is measured by action, not intention. Boards that can clearly demonstrate how and why decisions were made are not only better protected under the law, but also more effective in practice. Embedding disciplined judgement processes is essential to managing liability, maintaining credibility, and making decisions that stand up to scrutiny.
- Is our business judgement based on adequate information?

GHANA

Law and Practice

Contributed by:

Victoria Bright and Maxwell Amihere

Addison Bright Sloane



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Addison Bright Sloane is a full-service business law firm based in Accra, Ghana. The firm has provided tailored services to local and international corporations requiring the expertise of a law firm with in-depth knowledge of both the African business landscape and the ever-evolving global business environment. The firm's team of commercial and corporate lawyers comes with a diverse and rich corporate law practice portfolio across various industry sectors. Addison Bright Sloane is the partner of

choice for a top-tier global law firm and regularly collaborates with it and other international law firms on a number of high-profile transactions. Addison Bright Sloane regularly advises corporate clients on complex transactions and disputes. It has carved a niche for itself in M&A, ESG, infrastructure and projects, mining, energy, technology, privacy and data protection, environmental law, private equity, banking and finance law as well as dispute resolution (including international ADR).

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The principal forms of corporate/business organisations in Ghana are the following.

Partnerships

A partnership is an association of two or more individuals incorporated to carry on business jointly for the purpose of making profits. Partnerships are governed by the Incorporated Private Partnership Act, 1962 (Act 152).

Companies

One or more persons may form a company. Companies are governed by the provisions of the Companies Act, 2019 (Act 992). A company may be limited by shares, limited by guarantee or unlimited. It could be public, private or an external company.

Unincorporated Association

This is a registered association under the Companies Act, 2019 of individuals that have come together for a common purpose. Unlike companies, unincorporated associations lack a distinct separate existence.

1.2 Sources of Corporate Governance Requirements

The principal legislation in this area is the Companies Act, 2019 (Act 992). This new Act, replacing the Companies Act, 1963, represents a significant step forward in corporate governance standards for companies operating in Ghana. The Incorporated Private Partnership Act, 1962 (Act 152) (as amended) provides for the incorporation and registration of partnerships. It requires partnerships, inter alia, to keep proper books of accounts of their operations. The Corporate Insolvency and Restructuring Act, 2020 (Act 1015) provides the regulatory framework for distressed companies through stipulated systems for temporary management and restructuring of the otherwise distressed outfit.

More industry specific legislation includes:

- the Securities Industry Act, 2016 (Act 929) and the Securities and Exchange Commission Regulation, 2003 (LI 1728) (Act 929): the Act establishes the Securities and Exchange Commission (SEC), with its mandate to regulate, innovate and promote the growth and development of an efficient, fair and transparent securities market;

- the Banks and Specialised Deposit-taking Institutions Act, 2016 (Act 930) and the Insurance Act, 2021 (Act 1061), and their respective regulations;
- the Professional Bodies Registration Act, 1973 (NRCD 143);
- the Statutory Corporations Act, 1964 (Act 232);
- the Ghana Investment Promotion Centre Act, 2013 (Act 865); and
- the Stock Exchange (Ghana Stock Exchange) Listing Regulations, 1990 (LI 1509).

Additionally, there are a plethora of best practices often adhered to by companies that have been embedded into Ghana's corporate governance system over the years. For instance, internal auditors play a vital role in the corporate governance process even though companies are not required by law to hire them. Most of these best practices crystallised into statute when the new Companies Act, 2019 was passed. Internal audits serve as internal checks of a company, including its management and accountability procedures.

Similarly, the Companies Act, 2019 specifies a range of persons that qualify to act as a company secretary. However, most companies prefer qualified lawyers in good standing with the Ghana Bar Association to act as such. These practices help to ensure adherence to existing legislation and regulations.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Public companies are required to publish their audited financial statements, depicting the fiscal performance of the company and listing its majority shareholders at the end of each financial year. Only a public company may invite the

public to acquire shares. A public company may only do so after filing its prospectus with the Registrar.

This requirement is strict, and, consequently, any invitation made to the public in violation thereof constitutes an offence and offending persons could be criminally liable. In addition, the SEC has issued some guidelines to aid the process of issuing securities to the public, including that:

- the proceeds of any public offer/rights issue are to be used in strict accordance with the purpose(s) indicated in the offer document;
- the SEC will continue to undertake post-IPO/post-rights issue inspections to ascertain whether proceeds of the IPO/rights issue have been/are being utilised as indicated in the offer document; and
- issuers are required to disclose all fees to be paid out to persons or bodies in pursuance of the IPO/rights issue.

Further to this, characteristically, directors of public companies are voted or elected into office at a general meeting of the company. At the first annual general meeting (AGM) of a public company, by law, all directors (save an executive director) must retire. Following this, at all subsequent general meetings of the company, one third of the directors must retire on a first-come, first-go basis.

Public companies are also prohibited from extending loans, granting guarantees or providing security for loans to directors of the company or a director of an associated company.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Corporate governance rules and regulations are mainly contained in the Companies Act, 2019 (Act 992), which vests in the Registrar of Companies the power to ensure compliance with its provisions. First and foremost, every entity must be registered with the Registrar of Companies to be a legitimate corporate entity. The proposed name of the Company must not be misleading or undesirable and must include either of the following suffixes: limited company (ltd), public limited company (plc), limited by guarantee (lbg), public unlimited company (pub), private unlimited company (purc).

All companies must have at least one shareholder and not more than 50 shareholders for private companies. The biodata of beneficial owners of all registered companies must be provided to the Registrar of Companies (see the [Ghana Trends and Developments](#) chapter on the subject of beneficial ownership in this guide). Every company is required to have at least two directors who must qualify to be directors and consent in writing to act as such before their appointment (see **4.1 Board Structure** for more on directors).

To enhance corporate governance in the country, directors are required to act in the best interest of a company as a whole, function to preserve the company's assets, and generally act to further the business and promote the purposes for which the company was formed. The law enjoins them to do this in a faithful, diligent, careful manner such as is expected from an ordinary skilful director in given circumstances.

From Act 992, directors are further enjoined to have regard to:

- the likely long-term consequence of any decision they make;
- the impact of the operations of the company on the community and the environment; and
- the desirability of the company maintaining a reputation for high standards of business conduct.

A director who commits a breach of any of these duties is liable to some form of sanction, including:

- compensating the company for any loss resulting from the breach;
- accounting for profits realised from the wrongful transaction; and
- the rescission of the offending contract.

In addition to directors, the rules require every registered company to have other officers, such as an auditor and a secretary, and also to provide mechanisms for ensuring that officers and directors are accountable to shareholders, for example through the holding of AGMs (see **4. Directors and Officers**).

Most recently, the Supreme Court clarified that the erstwhile requirement of Act 992 for intending directors to declare, as part of a number of statutory declarations, whether they have been charged with a criminal offence, violates the constitution. In its decision in the case of *Derrick Adu-Gyamfi v The AG* (November 2023), the Court adjudicated thus: *"From the foregoing, we are of the view that the words 'charged with or' which appear in sections 13 (2)(h)(i), 13 (2)(h)(ii) and, 172 (2)(a)(i) & (ii) of Act 992 are inconsistent with the letter and spirit of Article 19 (1) & (2) of the 1992 Constitution and are accordingly void. The said words are unconstitutional and are hereby struck down."*

Acts Pertaining to Governance

Act 992 prescribes that companies should file annual returns once every year with the Registrar of Companies. Companies must maintain audited accounts, financial statements and reports (see **6.1 Financial Reporting**). With a view to preserving and maintaining the stated capital of the company, the Act further characterises certain transactions as major transactions (see **3.2 Decisions Made by Particular Bodies**). A special resolution by the members of the company is required to authorise such transactions.

Further, the central bank, in accordance with Section 56 of the Banks and Specialised Deposit-taking Institutions Act, 2016 (Act 930), published additional corporate governance directives in March 2018, establishing that:

- the term of office of a managing director or chief executive officer (MD/CEO) of a regulated financial institution shall not be more than four years and may only be renewed for an additional two terms;
- financial institutions are required to give an indication to the Bank of Ghana (BOG) of their achievements in terms of corporate governance goals within 120 days of the end of a financial year; and
- former officials of the BOG are prohibited from serving as directors of banks until the expiration of two years from their departure from the central bank.

The BOG also promulgated rules relating to persons who are not “*fit and proper*”, and corporate governance involvement is proscribed for such persons.

2.2 ESG Considerations

There is no obligation on companies to routinely report on environmental or social issues. The

Environmental Protection Agency Act, 1994 (Act 409) does, however, require a company to submit an environmental impact assessment report to the Agency, reporting on activities that might negatively impact the environment.

In addition, the Ghana Carbon Registry has recently been set up to receive, process, record and store data to be utilised for a range of purposes, including collecting and tracking transactions from mitigation activities at various levels.

The eligibility criteria for a project at the Ghana Carbon Registry establishes that:

- the project should be in the Nationally Determined Contributions (NDCs) programmes of action;
- the project should be part of the conditional NDCs programmes of action;
- the project should be in the whitelist (the whitelist contains eligible automatically additional technologies that are available for internationally transferred mitigation outcomes (ITMOs)) transactions at any given time; and
- the project should meet the criteria of the buyer.

The NDCs are programmes of actions which focus on minimising emissions, conserving the forest and dealing with climate change issues.

Regarding harmful emissions, the requirements are that any mitigation activity employed by a company that falls outside the scope of Ghana's NDCs programme may still be eligible to participate in the programme if:

- the related activity is covered by the latest National Greenhouse Gas Inventory prepared under the applicable Intergovernmental Panel on Climate Change (IPCC) Guidelines; and

- the activity is agreed upon by the participating acquiring party.

Finally, under Section 128 of Act 992, directors are also required to circulate to the members of the company the company's financial statements, a report by the directors and a report by the auditors. The financial report must include the emoluments of the directors and pensions of present and past directors. The directors' report must contain certain details such as the state of affairs of the company and corporate social responsibility.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The law provides that a company shall act through its shareholders in a general meeting or its board or through officers or agents appointed by either the board or the shareholders as per Section 144 of the Companies Act, 2019 (Act 992).

Members (Shareholders)

A person can become a member of a company by subscription, agreement, transfer of shares and by operation of law. Members of a company need not necessarily be natural persons. A member's right may be personal or collective.

Board of Directors

Being the body to whom the members (shareholders) of the company have entrusted the affairs of the company, the board constitutes the overarching team charged with ensuring the overall health and success of the company. Directors are appointed to direct and administer the business of the company. Unless a company's constitution stipulates otherwise, the busi-

ness of a company is managed by its directors or their delegates.

Officers

Act 992 defines an officer in relation to a body corporate to include any director, secretary or employee of that body corporate, receivers and managers whose appointment is authorised by the company and duly appointed liquidators.

3.2 Decisions Made by Particular Bodies Shareholders

A company acts through its members at a general meeting. The meeting may be an AGM or an extraordinary general meeting. Members in a general meeting are responsible for:

- the declaration of dividends recommended by directors;
- the appointment and removal of directors;
- effecting alterations to a company's constitution;
- fixing remuneration of auditors; and
- the appointment and removal of auditors.

In addition, "*major transactions*" require shareholder approval. Major transactions, as characterised by Act 992, are:

- the acquisition of, or an agreement to acquire, whether contingent or otherwise, assets, the value of which is more than 75% of the value of the assets of the company before the acquisition;
- the disposition of, or an agreement to dispose of, whether contingent or otherwise, assets of the company the value of which is more than 75% of the value of the assets of the company before the disposition; or
- a transaction that has or is likely to have the effect of the company acquiring rights or interests or incurring obligations or liabilities,

including contingent liabilities, the value of which is 75% of the value of the assets of the company before the transaction.

Board of Directors

The following decisions are taken by the board:

- deciding the company's major policies;
- ensuring and monitoring the financial integrity of the company;
- determining the company's capital structure;
- setting compensation for management; and
- proposing dividends payable per share.

These duties are to be performed by all or some of the directors on behalf of the entire board and for the company. Act 992 stipulates that the board acting within its powers is not bound by the instructions of the members in a general meeting. Minutes of its meetings are to be taken and kept and must be signed by the chairperson of the board.

3.3 Decision-Making Processes

The rules regulating decisions made by directors are usually found in a company's constitution and these include the requirements for meeting and voting, and the stipulated quorum for a directors' meeting. Decisions of the board are made at meetings by majority vote. Act 992 allows decisions to be made by directors without the necessity of attending a board meeting. In such instances, a written resolution signed by all directors shall be valid and effectual as if same was made at a duly convened meeting.

Decisions (crystallised into a resolution) are taken by members of a company at general meetings and all members are eligible to attend general meetings and vote at such meetings. Resolutions passed at general meetings are binding on all members as well as the company itself. Gen-

eral meetings may be convened by directors, members or the Registrar. A member is entitled, upon notice to the company, to appoint a proxy to attend and vote on their behalf at a meeting.

4. Directors and Officers

4.1 Board Structure

In contrast to some jurisdictions that have a supervisory board as well as a management board, boards in Ghana are based on a single-tier structure. A board may consist of both executive and non-executive directors who manage the business of the company and are appointed for a fixed term. The minimum number of directors in any company, whether public or private, is two with no maximum specified.

In the case of a vacancy (that is, a director is absent and cannot fulfil their duties), the remaining directors can continue to act, except where their number is reduced to one (or below the minimum number required by the company's constitution).

It is not mandatory for directors to hold company shares unless the constitution of the company specifies otherwise. Directors may appoint substitute and alternate directors, who must abide by the requirements set out in Act 992 and the company's constitution, and at least one director must be ordinarily resident in Ghana at all times.

4.2 Roles of Board Members

Board members are not given specific roles; however, in practice, directors could take on specific tasks. For example, they could serve on subcommittees of the board: as these are designated committees (handling specific issues such as audit, risk and governance), directors

would be functioning within the role assigned to them in that committee.

4.3 Board Composition Requirements/Recommendations

The Companies Act, 2019 (Act 992) requires that each board has a minimum of two directors. The Act recognises various categories of directors, including substitute directors, alternate directors, executive directors and managing directors. The board must have a company secretary who, though not a director (excepting cases where a director doubles up on the role), works with the board to navigate the corporate governance framework and ensure the company adheres to it.

Finally, the board includes a chairperson. This is a director who is appointed by the other directors to lead the board and preside over meetings.

It is a worthwhile recommendation to maintain a mix of professionals in the board's composition. For instance, accountants/financial types, lawyers, at least one relevant industry specialist, and those with experience in the human resources or IT sectors. For efficiency and attention to detail, board committees are useful. Another recommendation is for the board to have an uneven number to avoid a gridlock. Where an even number exists, the chairperson is usually given a casting vote.

4.4 Appointment and Removal of Directors/Officers

Directors are appointed by members at a meeting (except where there is a single member situation) and are removed at the AGM. Act 992 states that directors are appointed by shareholders and also stipulates that *"the constitution of a company may also provide for the appointment*

of a director/directors by a class of shareholders, debenture holders, creditors, employees or any other person". Prior to their appointment, prospective directors must declare that:

- within the preceding five years, they have not been charged with or convicted of an offence involving dishonesty or fraud;
- they have not been a director or senior manager of a company that has become insolvent; and
- they have not been charged with or convicted of a criminal offence relating to the incorporation and promotion of a company.

A company can remove any or all directors from the board if they have been disqualified from acting in that capacity. Directors are removed by ordinary resolution at a general meeting by the shareholders. Regarding public companies, the law requires a mandatory retirement of one third of the board annually on a first-come, first-go basis.

Act 992 stipulates that *"resolution to remove the director shall not be moved at a general meeting unless notice of this resolution has been given to the company a minimum of 35 days before the meeting at which the resolution is to be moved"* (Section 176, Act 992). The board may remove the company secretary, without prejudice to the secretary's right to damages where a breach of contract is occasioned in so doing.

4.5 Rules/Requirements Concerning Independence of Directors

Directors must disclose to the company any potential conflict of interest between themselves and the company. Such information, disclosed in writing or at a meeting of the board, will be recorded in the Interests Register. Failure to make this disclosure attracts a fine of 250 to

500 penalty units (one penalty unit is equal to USD0.78/GHS10.15 as at 13 June 2025). Act 992 further requires directors to exercise independent judgement. In addition, they are precluded from use of their positions or company's money/property except for the prescribed usage listed in Act 992 or the company's constitution.

Further, directors may not utilise for personal gain any confidential information obtained in their capacity as director, and must not be (in) directly beneficially interested in a business which competes with that of the company, nor have personal (in)direct interests in any contract or transaction other than those provided for in the Act 992.

Accordingly, unless a company consents (and superseding any company constitution that so allows), a director shall not place themselves in a position in which their duty to the company potentially conflicts with their personal interest(s) or duties to other persons. The law makes exceptions: the duty of a director to avoid conflict is not infringed if they have the board's consent, have fully disclosed their interests early on, and have not voted in any board meetings pertaining to the decision in which the director does have an interest. Provided they have the company's consent, a director may enter into a potential conflict of interest relationship to the company, notwithstanding potential legal fall-outs, for example a derivative action.

Regardless of its public or private status, consent by the company is mandatory in this context. In private companies, this can be done when there are no provisions in the company's constitution prohibiting authorisation. For public companies, authorisation can be given if the company's constitution permits the board to authorise the action.

4.6 Legal Duties of Directors/Officers Directors

Directors stand in a fiduciary relationship towards the company. As they hold a position of trust, directors are expected to act in good faith and in the best interest of the company at all times. This involves preserving the company's assets as well as furthering the company's business interests. For instance, they are prohibited from taking the company's assets for personal benefit.

The standard expected of directors encompasses the necessity to consider the consequences of any actions they take, and maintain high standards and a good brand reputation. According to the Second and Third Schedules to the Companies Act, 2019, the directors shall manage the business of the company. During the pre-incorporation stage, they are authorised to make payments from the company's coffers for all expenses incidental to promoting and registering the company.

Directors exercise the powers of the company, including borrowing money, charging property and the issuance of debentures. Directors are entitled to enter into a contract with the company, notwithstanding the need to maintain independence as provided in Section 192 of Act 992. The Act further states that such contracts cannot be avoided, nor shall a director be made to account for profit from it, merely for the director being in a fiduciary relationship with the company.

The board may appoint one among them to any other office in the company, including that of managing director, save the office of auditor. The directors can also revoke that appointment.

Secretaries

To qualify as a company secretary, an appointee should have obtained a professional qualification that provides them the relevant experience and knowledge to execute their duties. Such an appointee should either be enrolled to practice and be in good standing as a barrister or solicitor in Ghana, be a member of a professional body or have the requisite academic qualifications necessary for the role. Alternatively, they should have held office prior to the appointment, as a company secretary trainee, or have worked under the supervision of a qualified company secretary for at least three years.

Moreover, an appointee in good standing of the Institute of Chartered Accountants Ghana or the Institute of Chartered Secretaries and Administrators qualifies to be a company secretary. Unless the company's constitution provides otherwise, the company secretary shall be appointed by the directors. The statutory duties of the company secretary include:

- assisting the board to comply with the constitution of the company;
- keeping the books and records;
- ensuring the meeting minutes are properly recorded as required by the Act; and
- preparing and issuing notices in the name of the company.

4.7 Responsibility/Accountability of Directors

The directors are accountable to various stakeholders, namely, the company as an entity, the shareholders and the Registrar General. The Companies Act, 2019 (Act 992) provides that directors hold a fiduciary relationship with the company and are mandated to act in the company's best interest. They must also consider the impact of their actions on the shareholders,

the employees of the company, the community at large and the environment.

When appointed by a special class of members, employees or creditors, directors may “*give special but not exclusive consideration*” to their interests as well (Section 190). Directors are also accountable to the Registrar General's Department, as they can be penalised for misrepresenting themselves or for providing false information. Finally, they can also be prosecuted for criminal offences they were responsible for, had knowledge of or were complicit in.

4.8 Consequences and Enforcement of Breach of Directors' Duties

When a director breaches their duties, the director and any other person who knowingly committed the breach must compensate the company for any loss the company suffers as a result. The director shall also disclose any profits made from the wrongful transaction. Finally, the company reserves the right to terminate any transaction or contract entered into between the director and the company, in breach.

Where there has been a breach, the company or member of a company (ie, shareholders) can institute legal proceedings to enforce liabilities, restrain a threatened breach or by recovering property from the director. A company can do the above on the authority of the board of directors, a receiver and manager or liquidator, or via an ordinary resolution of the company which has been agreed to by the members. A legal challenge can also be brought in the form of a representative action by a class of shareholders with leave of court.

Another legal option open to shareholders and directors is a derivative action. After seeking leave from the court, any of the above parties

can bring a derivative action in the name of the company against any party (including another director of the company). Wilfully providing a false statement to the Registrar General is an offence liable to a fine.

The enforcer of these sanctions is the Registrar of Companies.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

A director's liability for their actions can be limited to the extent they comply with the company's constitution, the Companies Act, 2019 and by generally performing their duties to the best of their ability.

A director's failure to live up to their responsibilities may leave them open to legal liabilities. The following are some bases for a directors' liability:

- breaching of fiduciary interest;
- failing to act in the company's best interest;
- failure to adhere to the company's constitution;
- acting outside the limits of their power;
- making biased decisions;
- failing to disclose potential conflicts of interests or placing themselves in potentially conflicting positions without the company's consent; and
- making false declarations to the Registrar General.

Subject to the above, shareholders, other directors (via derivative action) or the company itself can institute legal proceedings against directors.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Shareholders fix the remuneration for directors. Aside from their allowances, directors are entitled to be reimbursed for expenses incurred in the process of executing their duty as directors (attending meetings on the company's behalf or other company-related business). Furthermore, a company's constitution may cater for compensation, including insurance benefits, where the tenure of a director is terminated.

In the case of a director losing their office, compensation must first be approved by the shareholders.

In the event of a takeover, if a director (who owns shares) is offered a higher price for their shares than other shareholders, the director must ensure that this fact is included in the notification sent to other shareholders.

Finally, compensation for directors is subject to income tax.

4.11 Disclosure of Payments to Directors/Officers

Companies must issue financial statements, which include an auditor's report. Amongst other things, the financial statements must disclose information on how much the directors are paid, along with any pension entitlements, and the emoluments of past and present directors in respect of loss of office.

Directors' fees must also be disclosed to the tax authorities (the Ghana Revenue Authority) as an income.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Act 992 specifies that a shareholder is a member of the company. As a result, shareholders collectively own the company, which confers on them the right to appoint directors. Membership of a company registered with shares continues until a valid transfer of the shares held by the specific member is registered by the company. Shares are transferred by operation of law to another person or forfeited for non-payment of calls, or on death of a member.

Shareholders have the right to attend and vote at AGMs. Subject to the company's constitution, the right to vote may depend on whether members have paid any sums of money required in respect of the shares allocated to them. Companies are also required to keep a register of members within the jurisdiction; this will be managed by the company secretary and includes the names, addresses and, where relevant, a statement of shares held by each member.

Shareholders can act for the company through general meetings, alongside the board of directors, officers and agents. Notably, unless the constitution of a company provides otherwise, the board of directors is not bound to comply with the directions of the shareholders. Furthermore, shareholders may act in a matter if the members of the board are disqualified, stuck in a deadlock, or otherwise. They may institute legal proceedings in the name of the company if the board of directors neglects to do so, can ratify or confirm an action taken by the board of directors, and can make recommendations to the board of directors.

The shareholders, moreover, can exercise their rights further by passing a written resolution signed by all members eligible to vote, outside a general meeting. However, this procedure is not valid where the object relates to the removal of a director or auditor. The latter can only be effected by a resolution passed at a general meeting.

The Office of the Registrar of Companies (ORC) maintains records of registered companies, including information about shareholders. Shareholder details are available to the public upon request through a formal search process. A company search at the ORC is conducted by submitting a formal request and the payment of the applicable fee.

5.2 Role of Shareholders in Company Management

Shareholders may exercise the powers given to them in the company's constitution with regard to company management. However, except as specified in the company's constitution, the board of directors largely manages the business of the company. Shareholders have the right to attend the company's general meeting and speak and vote on resolutions at the meeting; they also have the power to appoint and remove auditors and directors. In the event of a company winding up, shareholders must pay the balance of the shares they hold in accordance with the terms of the agreement under which the shares were issued.

In the event of a winding-up, shareholders are required to contribute funds sufficient for the payment of debts and liabilities of the company and for the expenses of the winding-up. According to Section 40 of Act 992, past members are not liable to contribute to the latter unless a court finds that the existing members are unable to satisfy the required contributions.

In the general management of the enterprise, shareholders have the power to approve “*major transactions*” (see 3.2 **Decisions Made by Particular Bodies**). Companies can only enter these transactions if approved by special resolution of the shareholders. Should any shareholder vote wholly against the transaction, that shareholder is entitled to have their shares bought, if they elect to sell. Shareholders can also approve compensation and retirement packages for auditors and directors.

5.3 Shareholder Meetings

AGMs are mandatory. Companies must hold an AGM each year, and designate it as such, so as to distinguish it from any other meetings held that year. AGMs must be held each year and not more than 15 months apart. However, if the company’s auditors and members (those entitled to attend and vote) agree in writing that the AGM shall be dispensed with in a given year, the company is allowed to waive the meeting for that year; if the meeting is not held due to the above reason, the Registrar of Companies may give directions as they deem fit.

Where meetings are called, 21 days’ prior notice must be given. The business of a meeting must be stated in the notice. Unless a company’s constitution says otherwise, shareholders are entitled to attend and vote at general meetings.

New Companies

A newly incorporated company has up to 18 months within which to hold the first AGM. Such AGM must be held at least 21 days after the company’s financial statements and the reports of the directors and auditors on the financial statements of the company have been sent to members and debenture holders of the company. These financial statements and reports shall be presented at the meeting.

When a company passes a resolution postponing the date of the AGM, a copy of said resolution must be forwarded to the Registrar. If an AGM is not held in accordance with the aforementioned conditions, the company is liable to pay an administrative penalty of 150 penalty units to the Registrar. Further, unless a company’s constitution states otherwise, members are entitled to vote by proxy. If it is unfeasible to conduct or call a meeting in the manner prescribed by the company’s constitution, either a director, member or the Registrar may apply to the court to conduct the meeting in a manner the court considers fit.

Shareholders

Shareholders are also entitled to attend extraordinary general meetings. Extraordinary meetings are convened at the board’s discretion, as well as when there are not enough directors within the jurisdiction capable of acting to form a quorum. Unless a company’s constitution states otherwise, these meetings will be held in Ghana.

Regardless of what may be stated in a company’s constitution, on the requisition of two or more members or a single member holding 10% of shares, a company can convene an extraordinary general meeting.

Minutes and Electronic Meetings

Section 166 of Act 992 provides that the minutes of general meetings shall be recorded in a book reserved specifically for that purpose. Minutes should be signed by the chairperson of the meeting (where a company defaults in this directive, the company and each officer therein is liable to pay the Registrar a penalty of 250 units).

A company shall circulate meeting resolutions and supporting circulars to members. The pro-

ceedings at these meetings are governed by the Companies Act, 2019 except for those sections in which provisions are made for governance by the company's constitution.

All meetings of the company can be conducted electronically. Similarly, the books and registers subject to inspection can be maintained in either electronic or manual format. The Registrar General has provided guidelines for the conduct of virtual AGMs of companies of which notice must be submitted to the head office in Accra or any of the regional offices. Notices of such meetings must be sent to every member electronically in accordance with the provisions of each company's constitution.

5.4 Shareholder Claims

A director's failure to live up to their responsibilities establishes the basis for claims against them. Examples of bases for claims include the following:

- breaching their fiduciary interest;
- failing to act in the company's best interest;
- failing to adhere to the company's constitution;
- acting outside the limits of their power;
- making biased decisions;
- failing to disclose potential conflicts of interests or placing themselves in potentially conflicting positions without the company's consent; and
- making false declarations to the Registrar General.

Subject to the above, shareholders can institute legal proceedings against the directors. They can also bring a representative action against the directors or apply for the leave of court to bring a derivative action.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Shareholders are not obliged to make general public disclosures of their holdings. However, they are required by tax laws to make disclosures of their earnings from investments in companies to the Ghana Revenue Authority for taxation purposes. Shareholders typically pay 8% income tax on their dividends.

Foreign directors are required to pay this too, unless their country has a dual-tax treaty with Ghana, in which case they may pay a reduced level of income tax. If the shares of a shareholder (or a group thereof) in a publicly traded company amounts to 35% or more of the total shares, they must disclose this to the remaining shareholders. It should also be noted that the names of majority shareholders are usually included in the mandatory publication of the notes to the audited financial statements of public companies.

The general threshold is that a person who has direct or indirect interest of 10% or greater in a company must be registered as a beneficial owner. For companies operating in the high-risk sectors, the threshold for reporting beneficial ownership is 5%.

Act 992 provides that every company is required to keep a register of members and beneficial owners and to furnish the Registrar General with the particulars of its members first at registration and subsequently to do so on an annual basis in its annual returns filed with the Registrar General. In the annual returns, the company is also required to indicate which of the beneficial owners are politically exposed persons.

The objective of providing particulars of beneficial owners, as well those who might be politically exposed persons, is to promote good gov-

ernance and accountability in companies and to support efforts to minimise and ultimately eradicate the risk of money laundering and consequential ills such as the financing of terrorism, financing the proliferation of weapons of mass destruction and other transnational organised crimes. The strategy also seeks to stem the flow of tainted monies into Ghanaian companies.

Section 13 of Act 992 provides that an application for incorporation of a company must include particulars of all persons who are beneficial owners. Where the persons who are recorded as shareholders of the company are not the beneficial owners of the shares, the company is required under Section 35 to also record the particulars of the beneficial owners of the shares in the Register of Members and to furnish the Registrar of Companies with these particulars within 28 days after being entered in the Register of Members. Particulars of beneficial owners are also to be provided in the company's annual returns filed pursuant to Section 126 of Act 992.

The Ghana Stock Exchange (GSE) requires shareholders in listed companies to release information to the public relating to their stock holdings at least 48 hours after the transaction occurs. The GSE's Listing Rule 55 stipulates:

- a person irrespective of nationality who purchases or sells shares in a listed company shall inform the market when their holding attains, exceeds or falls below each 5% threshold, starting from 10% through 15% and 20% up to 50% plus one share; and
- the disclosure shall be made in a press release to the market not later than 48 hours after the transaction.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Section 128 of Act 992 provides that directors are required to send three reports each year to members and debenture holders of the company. These reports are:

- the directors' report;
- financial statements; and
- the auditor's report.

The requirement is for the directors to send these reports at least once in every calendar year to all members and debenture holders of the company.

The Directors' Report

This is prepared by the directors and covers principally the company's corporate governance arrangements, the performance of the company during the year under review, and the outlook for the coming year. The corporate governance structures include organisation charts, committees of the board, profiles of board members, capacity-building initiatives for the directors and significant board decisions during the year. The business performance section covers the general economic environment, economic issues which impacted the company's performance, the performance of the company during the year and an outlook for the coming year.

The report shall discuss any changes in the business of the company (or of its associated companies), and also list the details of any subsidiary companies of the holding company. Inversely, if the company in question is a subsidiary, the report shall state details of the holding company. The report also discusses the corporate social

responsibility activities of the company and the expenditures of such programmes for the year.

The report must be approved by the board of directors and signed by two of them.

Company's Financial Statements

Directors prepare this in accordance with International Financial Reporting Standards (IFRS). These financial statements are:

- the statement of financial position;
- the statement of comprehensive income (including profit and loss);
- the statement of changes in equity;
- the statement of cash flows; and
- the summary of significant accounting policies and other explanatory notes to the accounts.

Consolidated financial statements must also be prepared for companies with subsidiaries (Section 131 of Act 992). Consolidated financial statements include statements on the company's financial position, consolidated comprehensive income, consolidated changes in equity, consolidated cash flows and notes about the consolidated financial statements.

The statements must give a true and fair overview of the profit and loss, comprehensive income statements and the general state of affairs within the company. Both the financial statements and the consolidated financial statements must follow the guidelines given in the Sixth Schedule to the Act.

The Auditor's Report

This is prepared by external auditors in accordance with international standards on auditing, as adopted by the Institute of Chartered Accountants, Ghana.

It is a report on the accuracy, completeness and fairness of the company's accounting records and financial statements, and must include specified items, such as whether the auditors received the necessary information and explanations for their audit, whether in the opinion of the auditors the accounts have been prepared according to the IFRS, whether they are true and fair representations of the underlying accounting records, and whether the auditor was independent of the company under audit.

6.2 Disclosure of Corporate Governance Arrangements

Corporate governance arrangements are disclosed as part of the regulatory reports expected from companies. See 6.1 Financial Reporting.

6.3 Companies Registry Filings

In Ghana, companies are incorporated and registered by the Office of the Registrar of Companies (ORC).

Companies are required to file annual returns with the Registrar of Companies. A notice that a company has filed its returns will be published in the Companies Bulletin published by the Registrar of Companies. There are no stipulations requiring the Registrar to make the returns themselves publicly available, but they are available for inspection.

Financial statements must not be published unless they have been approved by the board of directors and signed by two directors, and unless the directors' and the auditor's reports have been attached to them.

Publicly listed companies are additionally required to file their financial statements with the SEC and publish a summary of financial performance quarterly in national newspapers.

The Office of the Registrar of Companies (ORC) in Ghana has broad supervisory and regulatory powers under the Companies Act, 2019 (Act 992) to ensure compliance with corporate laws. It is responsible for registering and incorporating businesses, including sole proprietorships, partnerships and companies (both local and external), and issuing certificates of incorporation and commencement of business. The ORC regulates business names to prevent duplication or misleading registrations and oversees corporate governance practices.

Beyond registration, the ORC plays a key role in regulatory oversight by ensuring that companies file their annual returns, maintain proper governance structures, and update shareholder and director records. The ORC is responsible for collecting and collating information on business entities registered in the Business Register. Companies that fail to comply with statutory requirements risk being struck off the register. The ORC also has investigative and enforcement powers, allowing it to examine companies suspected of illegal or fraudulent activities. In cases of serious breaches, it can impose penalties, deregister companies or take legal action.

Additionally, the ORC discharges duties and performs functions of the Office as the Regulator of Insolvency Practitioners and is the Official Liquidator under the Corporate Insolvency and Restructuring Act, 2020 (Act 1015) and its Amendment, 2020 (Act 1031). It also supervises the liquidation and winding-up of companies, ensuring that businesses adhere to proper insolvency procedures and also appoints Inspectors, Receivers or Managers to ensure effective compliance with the Act.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

It is mandatory for a company to have an auditor. Where a company fails to appoint an auditor and continues to operate under default for a period beyond three months, the Registrar General is mandated to appoint one for that company. An appointed auditor must expressly consent to the appointment. Such a person or corporate entity must meet a set of qualification criteria.

The relationship between an auditor and the company is set out in Act 992. Once appointed by an ordinary resolution of shareholders, the auditor can be maintained for up to six years. Once disengaged, the same auditor cannot be appointed by that company until after another six years elapses.

A duty is placed on auditors to avoid conflict of interest situations in much the same way as directors. Primarily, the auditor must ensure that, in carrying out their duties, their personal judgement is not impaired by the existing relationship with or interest in the company or any subsidiary of the company.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The existence of a registered constitution with prior approved checks and balances operates to mitigate or regulate risks in the management of companies. Whilst not mandatory for a company to register a customised constitution, a company has the option to do so. However, where it chooses not to customise its constitution then the standard constitution set out in Act 992 becomes a default constitution. A constitution would ordinarily regulate such important matters as the numbers and meetings of directors, and

stipulate the dividend policy of the company and other important matters.

It so often happens that a cause for division among members of a company is with the payment of dividends. The cause of the division often emanates from the dual involvement of both the directors and the shareholders in the declaration and payment of dividends. Directors make the initial determination of whether or not dividends are payable in a given financial year and shareholders approve or confirm the dividend payment by ordinary resolution.

It is also required that certain resolutions obtain the court's blessing subsequent to having been passed by the company. Thus, for transactions such as the reduction of the stated capital of the company, the reduction of the unpaid liability on any shares, the return to shareholders of any assets or the cancellation of any shares (which requires altering the constitution), the resolution, after being passed, would have to be further confirmed by a court on application by the company.

Possible Criminal Implications

Directors have to conduct company business with the knowledge at all times that their actions could criminally implicate the company, and, further, that liability can attach to the company just as much as it would to a human. The scope of this risk becomes even more compelling when one takes into account the fact that the company would not be absolved of liability on the basis that a director (or shareholder or managing director) had acted fraudulently or forged documents in furtherance of the intent on the blind side of the company. Nevertheless, this is juxtaposed with the related understanding that not all acts of directors can implicate the company.

Thus, only where the board, shareholders (in a meeting) or the managing director has specifically authorised the particular officer (director) so to act would the malfeasance of that director (or officer) be attributed to the company. At a minimum, the individual director must be able to show some express communication assigning the authority to them at some point so to act, prior to undertaking the action. Consequently, it is in the interest of the board not to leave the status of any individual as to whether or not that individual is a director in limbo.

Ambivalence

By implication of this vicarious liability, any ambivalence carries with it the potential attendant risk of implicating the company. Moreover, it is a legal requirement also that a company has a minimum of two directors with at least one resident within the country at any given time. The requirement operates to preclude the volatile but plausible situation where all the directors are out of the country and the company is left to run without the proper corporate governance oversight expected from directors.

The law prescribes strict rules regarding the appointment, removal and (in the case of public companies) rotation of directors. This guards against the capricious usage of the power of appointment and removal to further selfish interests.

Company Well-Being

The managerial and oversight powers of directors are by no means unfettered. As discussed earlier (see 3.2 **Decisions Made by Particular Bodies**), there is a limitation on the powers of directors in the areas of borrowing, lending and contributions, as well as with the issuance of new or unissued shares, and entering into major transactions. Directors can only get such trans-

actions done subject to a resolution of the company.

To further buttress the elimination of potential conflict areas between the individual interests of directors and the company's well-being, the law strictly prohibits advancing loans to directors of public companies. The law categorically stipulates: *"A public company shall not grant a loan to a person who is a director or a director of an associated company or enter into a guarantee or provide a security in connection with a loan made to that person by any other person"* (Section 328 (1) of Act 992). This restriction is somewhat relaxed for private companies, which only need to specify the fact in the note to the financial statements of the company.

Certainly, the balancing act of managing risk while handling the affairs of a company can be dicey. Consequently, the courts may in given circumstances grant a reprieve. For instance, where a director has acted honestly, then, despite the occurrence of a breach in the execution of their duty, the court may either partially or wholly absolve the director of liability.

Trends and Developments

Contributed by:

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Addison Bright Sloane

Addison Bright Sloane is a full-service business law firm based in Accra, Ghana. The firm has provided tailored services to local and international corporations requiring the expertise of a law firm with in-depth knowledge of both the African business landscape and the ever-evolving global business environment. The firm's team of commercial and corporate lawyers comes with a diverse and rich corporate law practice portfolio across various industry sectors. Addison Bright Sloane is the partner of

choice for a top-tier global law firm and regularly collaborates with it and other international law firms on a number of high-profile transactions. Addison Bright Sloane regularly advises corporate clients on complex transactions and disputes. It has carved a niche for itself in M&A, ESG, infrastructure and projects, mining, energy, technology, privacy and data protection, environmental law, private equity, banking and finance law as well as dispute resolution (including international ADR).

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Introduction

Corporate governance is an ever-changing system of rules and practices designed to assist companies to achieve their objectives through efficient management and control of the company's operations. The passage of the Companies Act, 2019 (Act 992) and the issuance of directives by regulatory bodies such as the Registrar of Companies, the Bank of Ghana and the Securities and Exchange Commission have ushered in a new era of corporate governance rules designed to modernise the management of companies in the country. These regulations comprise provisions for the use of technology in company regulatory matters, increased duties for directors, and acknowledgement of minority rights of shareholders, amongst others. This chapter of the guide will discuss the prominent trends and developments in the corporate governance space, for the most part occasioned by the passage of Act 992.

Any discussion of the most notable developments and trends in corporate governance in Ghana must include the following.

Establishment of the Office of the Registrar of Companies

Harkening back to the original intent of the drafters of Ghana's first Companies Code 1963, the country now has a new statutory body, namely, the Office of the Registrar of Companies and a separate office of the Registrar General. The office of Registrar of Companies (headed by the Registrar of Companies) is responsible mainly for the registration and regulation of all types of businesses in Ghana. The office also oversees the registration of business names, registration of partnerships, appointment and regulation of company inspectors. This would now be distinguished from the responsibilities of the Registrar General's Department, the latter now dedicated to the registration of intellectual property rights, marriages and administration of estates. Additionally, it functions as the Official Liquidator of Companies, and manages the finances and fixed assets of the Office of the Registrar. The Registrar is appointed by the President of Ghana and performs his functions with the assistance of a governing board. The Registrar, in addition to his duties, is expected to issue guidelines periodically to companies on the conduct of their operations.

The Office of the Registrar has been created in accordance with the Companies Act, 2019 (Act 992). Following this, in July 2022, the President of Ghana officially launched the Office of the Registrar of Companies (ORC).

Enhanced Corporate Governance Requirements for Directors

The role of directors has come under immense scrutiny following the collapse of a number of banks and non-bank financial institutions in the country. This compelled the regulator, Bank of Ghana, to issue the current corporate governance directives for banks and non-bank financial institutions, which brought in much-needed institutional changes.

Further to this, the Bank of Ghana issued a Ghana Corporate Governance Disclosure Directive (May 2022), which applies to Regulated Financial Institutions (RFIs). The objectives of this Directive are as follows:

- to enhance transparency and market discipline;
- to enhance the accountability of the RFI to its stakeholders;
- to assess the effectiveness of RFIs' corporate governance practices and their risk profiles;
- to promote public confidence and trust in RFIs; and
- to amend all disclosures required in the RFIs' Annual Reports.

Similarly, the Securities and Exchange Commission has issued directives governing the conduct of affairs of publicly listed companies.

Act 992 and other corporate governance rules have raised the qualifying criteria, duties and liabilities of persons appointed as directors of companies. The objective is to weed out per-

sons whose involvement could be inimical to the growth of enterprises, or at a minimum keep their actions in check. For instance, in addition to the qualification requirements for directors under the Companies Act, 2019, the Bank of Ghana has set out additional criteria for directors and key management personnel of banks and other financial institutions. Under the Bank's directive, a person appointed as a director must be a fit and proper person. "*Fit and proper*" means the person is suitable to hold the particular position as regards:

- the probity, competence and soundness of judgment of that person for purposes of fulfilling the responsibilities of that person;
- the diligence with which that person fulfils or is likely to fulfil those responsibilities;
- whether the interest of depositors or potential depositors of the entity is threatened, or likely to be in any way threatened, by the person holding that position; and
- the integrity of the person being established and the qualifications and experience of the person being appropriate for the position in the light of the business plan and activities of the entity that they serve, or are likely to serve, taking into account the size, nature and complexity of the institution.

In addition to previously existing responsibilities, stringent liabilities underpin the performance of directors' duties to ensure proper management and accountability of directors towards companies. The extent of the power exercised by directors is also circumscribed by Act 992 and made subject to the constitution of the company. For example, without a prior resolution of the company, directors may not issue new or unissued shares or contribute to any charitable fund other than a pension fund. Similarly, a contract or transaction classified as "*major transaction*"

under Act 992 requires a special resolution of shareholders before its execution by the company's directors. Directors are liable for breach of their duties. Such liability includes compensating the company for any loss occasioned to it. Moreover, Act 992 precludes any attempt to exclude such liability either through express provisions in the company's constitution or by agreement between a director and the company.

A National Corporate Governance Code was launched by the Institute of Directors, Ghana in partnership with Bank of Ghana and other key stakeholders. The intent is for this code to serve as a unified national corporate governance reference for all stakeholders both in the public and private sectors in the country.

Enhanced Corporate Governance in Public Organisations

The State Interests and Governance Authority (SIGA) and the Public Services Commission (PSC), in collaboration with the Ministry of Finance and the Public Enterprises Secretariat, issued the Code of Corporate Governance for Specified Entities and Public Service Organizations in Ghana, dated June 2023, with the purpose of providing guidance to transform the corporate governance practice systems in specified entities and public service organisations.

The code acts as a framework that provides guidelines by which boards and management of public organisations can execute their roles and responsibility to have good oversight of the organisation and manage their performances to yield the best performances for the benefit of their organisations and the state overall. The code hopes to achieve this mandate by encouraging proactive measures and ethical and pragmatic decision-making by all players and stakeholders.

Enhanced Qualification of Company Secretaries

As part of the corporate governance enhancement provisions under Act 992, companies are required to appoint only duly qualified persons to serve as company secretaries. The minimum threshold includes:

- holding a tertiary level education with a corporate secretary bias;
- previous service under a qualified company secretary for at least three years; or
- being a member in good standing of the Institute of Chartered Secretaries (Ghana) or the Institute of Chartered Accountants (Ghana), or enrolled to practise as a solicitor or barrister in Ghana.

The predominant practice is for most companies, particularly SMEs and large corporations, to opt for a qualified lawyer to fill this role in spite of the above breadth of qualifying criteria.

The Concept of Beneficial Ownership

This is a new concept, without any historic antecedence. It has evolved out of the government's drive to stem systemic corruption and money laundering. This is designed to improve transparency in company profiling with a view to ascertaining persons actually controlling a company. It has been a common practice in Ghana for companies to hide the actual owners and instead present ostensible shareholders for a range of reasons. Under penalty of law, this new development makes it mandatory for registered companies to make available to the Registrar of Companies the bio data of actual owners and "*beneficial owners*" under Act 992, and to indicate persons considered "*politically exposed persons*". A beneficial owner is an individual:

- who directly or indirectly ultimately owns or exercises substantial control over a person or company;
- who has a substantial economic interest in or receives substantial economic benefits from a company whether acting alone or together with other persons;
- on whose behalf a transaction is conducted; or
- who exercises significant control or influence over a legal person or legal arrangement.

The definition of “*politically exposed person*” includes a person who is or has been entrusted with a prominent public function in Ghana, a foreign country or an international organisation.

There are different types of thresholds for reporting a beneficial owner of a company depending on the sector the company is in and the type of person the beneficial owner is. The general threshold is that a person who has direct or indirect interest of 10% or greater in a company must be registered as a beneficial owner.

Major Transactions

Additionally, there is a new requirement for shareholders to approve certain intended steps and decisions taken by the board before they come into effect. The current trend is to involve, as much as possible, the owners of the company in the taking and implementation of significant steps. These types of decisions are classified as “*major transactions*” under Act 992. The idea, inter alia, is to enhance corporate accountability, mitigate losses and safeguard the assets of companies. The Act defines “*major transaction*” as:

- the acquisition or the agreement to acquire assets the value of which is more than 75% of the value of the assets of the company;

- the disposition or agreement to dispose of assets the value of which is more than 75% of the value of the assets of the company; or
- a transaction where the company acquires rights or interests, or incurs obligations and liabilities, the value of which is more than 75% of the value of the assets of the company.

Shareholders who vote against a resolution to undertake “*major transaction*”, which resolution is passed in any event, have the option to request the company to buy them out.

Minority Rights

Act 992 grants specific remedies for minority shareholders who feel oppressed. In addition to the option open to shareholders to have their shares bought out after a vote on a major transaction (as discussed above), dissenting shareholders on a matter have the right to institute legal action in situations where they feel oppressed. Moreover, where the company has done or threatens to undertake an action that tends to discriminate against or is unfairly prejudicial to some of the shareholders, such shareholders may be entitled to a cancellation of such action by court order.

Further, to curtail dissension and prolonged litigation, Act 992 allows shareholders to opt out of the company where a company amends its constitution to vary the previous objects or business of the company. This also applies where a special resolution is passed approving a major transaction or an arrangement for a merger and acquisition or the variation of a class of shares is undertaken (against the shareholder’s will). The option for a buy-out allows minority shareholders to utilise remedies under Act 992 to protect their investments. No longer will minority shareholders who wholly vote against resolutions for

matters specified above continue to hang on with dissatisfaction and acrimony.

Additionally, minority shareholders have the option to enforce their rights through derivative actions. They may apply to the court for leave to institute proceedings in the name of the company or on its behalf to enforce their rights or recover the company's assets. Derivative actions present an existential avenue accessible by minority shareholders to hold the directors of the company accountable for their actions by leveraging the courts.

Electronic and Digital Transformation

As part of the government of Ghana's policy to digitise the economy, state institutions are mandated to employ digital transformation tools in the discharge of their duties. Thus, Act 992 empowers the Registrar of Companies to authorise certain transactions electronically through a digital platform approved by the Registrar. Some activities that can be done electronically include:

- the incorporation or registration of a company;
- the reservation of a company name;
- the filing of particulars;
- the filing of annual returns and financial statements;
- the keeping and maintenance of a register;
- the inspection of a register;
- the registration of debentures;
- the transfer of debentures;
- the registration of charges;
- the service of notice of a document;
- searches on a company register; and
- payment of fees.

These services and many others show the commitment of the Registrar to provide services through electronic platforms for companies.

Sundry Developments

Inspection of companies

To ensure compliance with the Companies Act, 2019 (Act 992) and pursuant to Section 35 of the Act, the ORC has begun a nationwide inspection of companies and businesses in all regions in Ghana. During these inspections, the ORC will inspect all documents including registration and incorporation certificates, the register of directors and members, and annual return filings.

Failure to comply with the provisions of the Companies Act will lead to sanctions by the office such as a fine of 150–250 penalty units or a term of imprisonment, or both, as stipulated in Section 35 (15) of Act 992.

Classification of companies

On 22 January 2025, the ORC issued a directive introducing important classification of companies under the Companies Act and Companies Regulations 2023 LI 2473 with the aim of streamlining compliance requirements and specific exemptions for small and medium-sized companies.

Companies are classified by the Companies Regulations into small, medium or large, based on their turnover assets and other variables. This is done by the Registrar in consultation with the Governing Board of the Office of the Registrar of Companies. This classification is to ensure that regulatory requirements match the size and capacity of each business.

The companies are classified as follows.

- Small companies are those with revenue or assets up to GHS400,000.
- Medium companies are those which fall within the range of GHS400,001 to GHS10 million.

- Large companies have revenue or assets exceeding GHS10 million.

Exemptions for small and medium companies

The apparent changes intended by this directive are exemptions afforded to small and medium companies regarding filing annual returns. These classes of companies are no longer required to submit a full version of their annual returns as mandated by Section 126 of Act 992. They are now only required to confirm the accuracy of the information in the Registrar's record, thus lessening the administrative workload for small and medium companies, affording them the benefit of improving their operational activities.

Notable among the exemptions is the exemption of small companies from audit requirements. The new directive exempts this class of companies from conducting audits or publishing financial statements as outlined in Section 137 of Act 992. They are now subjected to a limited review conducted by their internal auditors.

However, these reviews must comply with the following:

- the International Standards on Review Engagement (ISRE); and
- the standards issued by the International Audit and Assurance Standard Board (IAASB) for less complex entities as adopted by the Institute of Chartered Accountants, Ghana.

In order to enjoy the exemptions, qualifying businesses must ensure that their records with the Registrar are accurate and up to date to meet the confirmation requirements for the annual returns.

Small and medium companies stand to benefit from simplified processes, reducing the cost and

administrative drawbacks and allowing for more time to be invested in the business's growth.

Issuance of new certificates

As part of an initiative to improve service delivery, provide secure and reliable documentation and ensure the integrity of official documents to businesses and stakeholders, the ORC, on 13 March 2025, introduced the issuance of new entity registration certificates to companies.

The features of the new certificates include enhanced security measures, ORC logo, a seal and an improved design element. The ORC advised clients to apply for the new certificates with the enhanced features. This notwithstanding, all existing registration certificates remain valid and legally recognised, and businesses are not required to replace them unless necessary.

Enhanced Corporate Insolvency Rules

Lately, Ghana's corporate governance has welcomed a new entrant: the Corporate Insolvency and Restructuring Act, 2020 (Act 1015). This Act has ushered in an exciting and modern approach to insolvency aimed at rescuing companies in distress. This is timely as Ghana and the rest of the world battle an economic downturn.

As some businesses continue to struggle to stay afloat, the need to salvage otherwise viable businesses, and also secure creditor interest, has taken centre stage – hence the enactment of Act 1015.

Act 1015 covers virtually all industry types, except those classified as special industries such as banks and insurance companies. The highlights of the new Act include:

- the provision for administration or restructuring as an essential tool for companies in

- distress to continue in existence as a going concern;
- the provision of temporary management of the affairs, business and property of a distressed company; and
- in appropriate cases, the placement of a temporary freeze on the rights of creditors and claimants against the company.

These remedies were previously unavailable under the Bodies Corporate (Official Liquidation) Act, 1963 (Act 183), which only catered for winding-up procedures in the case where a company's liabilities exceeded its assets or it was unable to pay its debts.

The measuring yardstick for insolvency remains the ability or otherwise of a company to meet its financial obligations when they fall due. Act 1015 allows a distressed company some protection to reorganise its affairs without being burdened with the threat of liquidation from its creditors. The administration of a company begins when an administrator is appointed. Only a natural person can be appointed as an administrator and they must be duly qualified as an insolvency practitioner. The next stage after administration is for creditors of the company to execute a restructuring agreement. The restructuring officer (RO) has the responsibility to implement the restructuring agreement with appropriate notifications to the creditors and the Registrar of Companies. The restructuring agreement provides for the terms and conditions of the restructured debt such as moratorium period and payment plans.

Another novelty introduced by the Act is the introduction of the regime for insolvency practitioners as well as the insolvency division at the Office of the Registrar of Companies. Previously, there existed no professional regulator nor standards for insolvency practice. As a

basic prerequisite, a person is qualified to be an insolvency practitioner if that person is a chartered accountant, lawyer or banker who is in good standing with their professional association. The Registrar of Companies must also certify or license an individual as such. The law further requires practitioners to have the requisite professional indemnity insurance to enable them to practise as an insolvency practitioner. In December 2021, the Ghana Association of Insolvency Advisors (GARIA) and the Office of the Registrar of Companies ushered in the first batch of insolvency practitioners to help in the administration of businesses, properties and affairs of distressed companies in the country.

In the same vein, GARIA inducted the second batch of insolvency practitioners as part of the Office of the Registrar of Companies' objective to respond to the local needs of distressed companies. Plans are underway to ensure that the ORC is self-financing to carry out its mandate, which includes the establishment of the Insolvency Services Division.

The Insolvency Services Division was created under Act 1015 to regulate insolvency practice, oversee the administration, restructuring and insolvency proceedings of companies, and make recommendations to the Registrar on any changes deemed necessary to the relevant laws on insolvency in Ghana.

Another important feature of Act 1015 is the introduction of cross-border insolvency procedures. Cross-border insolvency proceedings have been established to promote co-operation between a court and other competent authorities of Ghana and those of foreign states involved in cases involving both or multiple countries. The provisions in the Act are reflective of the United Nations Commission on International Trade Law

(UNCITRAL) model law on cross-border insolvency. It allows for the recognition of foreign insolvency proceedings and reliefs. Operationally, a foreign representative can apply for the commencement of an insolvency proceeding in Ghana and participate in proceedings regarding a debtor or creditor.

Striking Down of Certain Sections of the Companies Act, 2019

The Supreme Court has recently clarified that the erstwhile requirement in Act 992 for intending directors to declare, as part of a number of statutory declarations, whether they have been charged with a criminal offence, violates the constitution. In its decision in the case of *Derrick Adu-Gyamfi v The AG* (November 2023), the Court held: *“From the foregoing, we are of the view that the words ‘charged with or’ which appear in sections 13 (2)(h)(i), 13 (2)(h)(ii) and, 172 (2)(a)(i) & (ii) of Act 992 are inconsistent with the letter and spirit of Article 19 (1) & (2) of the 1992 Constitution and are accordingly void. The said words are unconstitutional and are hereby struck down.”*

However, the Court stipulated in respect of the constitutionality of Section 177 (1)(c) and (e) as follows: *“We are however unable to agree with the Plaintiff’s submission that Section 177 (1)(c) & (e) are in breach of the constitutional provisions on fair hearing and presumption of innocence. We do not find the said provision to be inconsistent with Article 19 (1) and 19 (2)(c) and 15 (3) of the Constitution. Consequently, the reliefs sought by the Plaintiff in respect of section 177 (1)(c) & (e) are dismissed.”*

AI’s Role in Corporate Governance

Artificial intelligence (AI) is increasingly influencing corporate governance practices in Ghana, offering tools to enhance decision-making, risk management and compliance. While AI adoption is growing across various sectors, its integration into corporate governance frameworks is still developing.

AI and machine learning (ML) offer significant potential to transform traditional practices by automating data analysis and minute-taking during meetings. AI carries the potential to enable organisations to proactively identify risks and ensure adherence to regulatory standards.

Conclusion

The corporate governance space continues to be an active space admitting novel ideas and systems. The aforementioned are by no means exhaustive, representing instead the important highlights in an ever-changing corporate legal landscape. What remains certain is the intent of various regulatory bodies to continue to improve corporate governance in Ghana through ushering in new standards to improve efficiency overall.

GIBRALTAR



Law and Practice

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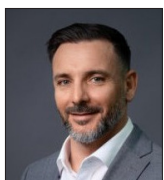
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ISOLAS LLP is a leading international law firm with its headquarters in Gibraltar. Established in 1892, it is Gibraltar's oldest law firm. The firm's lawyers bring disciplined and effective management to large, structured deals, whilst also remaining flexible and open to innovative opportunities. Delivering commercial solutions for clients across a range of industry sectors and jurisdictions, the team not only understands the company law framework, but also brings an international perspective that accommodates the common cross-border nature of global business

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Corporate vehicles in Gibraltar may take various forms. These include:

- foundations;
- limited partnerships;
- protected cell limited partnerships;
- limited liability partnerships;
- companies limited by guarantee (with or without a share capital);
- companies limited by shares;
- protected cell companies; and
- unlimited companies.

As each form of corporate vehicle contains its own unique set of characteristics, the most suitable vehicle for a particular use-case will depend on various factors, such as the nature of the underlying business activity or reasons for the establishment of the vehicle (eg, asset protection or succession planning).

Companies limited by shares are by far the most common form of corporate vehicle in use in Gibraltar. These may be set up as a private company (in which case the company's shares or debentures are not allowed to be offered to

the general public) or as a public company (in which case the company's shares or debentures are allowed to be offered to the general public).

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance requirements for companies in Gibraltar are the following:

Companies Act 2014

The Companies Act 2014 is the principal statutory instrument governing the formation, operation and dissolution (excluding companies in compulsory liquidation) of companies in Gibraltar.

Financial Services Act 2019

The Financial Services Act 2019 (FSA) and its accompanying sector-specific Regulations establish Gibraltar's regime for financial services and securities law. The FSA applies to any person who carries on a regulated activity in or from within Gibraltar. The FSA also establishes the restrictions that apply to an offering of securities to the public made in or from Gibraltar.

The FSA and its accompanying Regulations came into force on 15 January 2020, following the largest-ever reform programme of Gibraltar's financial services legislation, and provide a

modern legislative framework for all financial and professional service sectors in Gibraltar.

The reform consolidated approximately 90 pieces of legislation within an enhanced, more accessible and modernised structure, which introduces cross-sectoral terminology and powers for the Gibraltar Financial Services Commission (GFSC), aimed at ensuring consistency across all regulated activities.

The Regulations complement the new structure, concepts and terminology of the FSA by consolidating prudential business conduct and other requirements applicable to each financial service industry within respective sets of sector-specific Regulations.

Common Law

Common law relates to the body of uncodified laws based on legal precedents established by the courts.

The common law and the rules of equity from time to time in force in England and Wales apply to Gibraltar, subject to any modifications or exclusions made by His Majesty in Council, an Act of the UK Parliament or an Act passed by the Gibraltar Parliament pursuant to the Gibraltar English Law (Application) Act 1962.

While Gibraltar's legal system is based on that of England and Wales, Gibraltar's statute law has developed differently in so far as the Gibraltar Parliament has enacted and amended laws to suit Gibraltar's own particular requirements. Accordingly, it is important to note that English common law is not binding in Gibraltar but can be a highly persuasive authority in Gibraltar legal proceedings where the statutory background is sufficiently similar.

The fiduciary duties that directors owe to a company, for example, are products of common law and are not codified in statute.

Insolvency Act 2011

The Insolvency Act 2011 contains provisions relating to the insolvency and winding up of companies in Gibraltar.

Corporate Governance Code for Collective Investment Schemes

In 2013, the Gibraltar Funds and Investments Association (GFIA) introduced a Code of Conduct for Collective Investment Schemes (the "Code"), which was meant to address best practices in the context of experienced investor funds and private funds.

The Code captured existing accepted principles of good practice and guidance, and further developed these principles by capturing Gibraltar-specific issues such as the governance of self-managed funds and oversight of experienced investor funds structured as protected cell companies.

As well as dealing specifically with the role and responsibilities of a fund director, the Code seeks to set out directors' duties during each stage of the life cycle of a typical fund, and defines what is expected in respect of the effective oversight and supervision of service providers to the fund. It also covers specific elements of the composition of a fund's board and its collective skill set.

In 2018, through a specific addendum to the Code, Gibraltar became the first jurisdiction in the world to issue specific standards for the structure of crypto funds, including corporate governance, risk management, valuation, custody, safekeeping and security, and a host of other important touchpoints (the Corporate

Governance Code for Gibraltar Crypto Funds). Following the success of the first edition of the Corporate Governance Code for Gibraltar Crypto Funds, an updated second edition was published in March 2022.

It is important to note, however, that the Code is not legally binding and operates under the principle of “*comply or explain*” which is to say, the Code is not there to say how something must be done. The Code is there to encourage licensees to consider certain issues and, where the licensee feels that those issues are better dealt with in a different fashion, to document their thought process.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

In addition to the requirements discussed in 1.2 **Sources of Corporate Governance Requirements**, companies with shares that are publicly traded must also comply with the EU Market Abuse Regulation, which continues to apply in Gibraltar, subject to certain amendments introduced under the Financial Services (Market Abuse) (Amendment) (EU Exit) Regulations 2020 in order to address deficiencies and to ensure that the EU Market Abuse Regulation is able to operate effectively under Gibraltar law following Gibraltar’s withdrawal from the EU.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance Sanctions

By virtue of the Sanctions Act 2019 (the “Act”), international sanctions have effect in Gibraltar. Such measures include the application of:

- EU sanctions;

- UN Security Council sanctions;
- any restrictive measures imposed by means of a designation within the meaning of the UK Terrorist Asset-Freezing etc. Act 2010;
- any restrictive measures imposed by an organisation that is notified by the government by notice published in the Gazette; and
- any restrictive measures imposed by the UK under the Sanctions and Anti-Money Laundering Act 2018.

The Act therefore provides for the automatic recognition and application of any restrictive measures imposed by the UN, the UK and the EU. The implementation of such measures has had quite an impact on corporate governance, particularly since the recent events in Ukraine, and particularly for the legal and corporate service providers industry. When dealing with a Russian individual or corporation, or any person or entity connected with Russia, for example, service providers in Gibraltar have to navigate the different sanctions regimes imposed by the UN, the UK and the EU.

ESG

Additionally, the rise of environmental, social and governance (ESG) initiatives has seen an increasing number of firms taking measures to reduce their carbon footprint and in turn increase their economic sustainability in order to remain attractive in the legal market. ESG standards are a criteria used to ascertain the sustainability of the non-financial impact of investments. Firms have dedicated themselves to organising and setting up ESG teams in order to assist with the navigation of ESG disclosure requirements, which we are moving towards. See 2.2 **ESG Considerations**.

2.2 ESG Considerations

Under the Companies Act, a large company (as defined within the Companies Act) which is a

public-interest entity is required to issue a non-financial information statement within the directors' report. The information required by the statement must include information relating to:

- environmental matters (including the impact of the company's business on the environment);
- the company's employees;
- social matters;
- respect for human rights; and
- anti-corruption and anti-bribery.

The statement must also provide brief details of the company's business model.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies involved in the governance and management of a Gibraltar company can be broken down into shareholders, the board of directors and the secretary.

Shareholders

A company must have at least one registered shareholder, who may be either a natural person or a body corporate. A person, having agreed to become a shareholder, becomes a shareholder of a company upon their name being entered in the company's register of shareholders.

There is no limit on the maximum number of shareholders that a private company can have. The Companies Act had previously restricted private companies to a maximum of 50 shareholders. However, this restriction has since been removed, and private companies can therefore consist of an unlimited number of shareholders

without the need to be registered as a public company.

The company must record the details of the new shareholders in the register of shareholders.

Board of Directors

Directors are appointed to direct, control and supervise the activities and affairs of a company. Directors are a connecting line between the company and third parties. By definition, a director *"includes any person occupying the position of director by whatever name called"*. This definition is wide in order to include those who are effectively dealing with the affairs of the company, but who do not bear the title *"director"*. It also ensures that there is no legal distinction between executive directors and non-executive directors, although differences will usually be found in the roles they perform.

The conducting of board meetings is generally not covered by the Companies Act. The main statutory provisions affecting board meetings concern minutes of board meetings being kept and disclosure by directors of interests in contracts. The rules for conducting board meetings largely depend on the company's articles of association, thus giving a company great flexibility. For example, Gibraltar law does not prevent board meetings from being held anywhere in the world nor does it prevent directors from participating in board meetings through electronic means. However, a company must seek tax advice when doing so in order to mitigate any potential tax consequences.

Secretary

Every company incorporated in Gibraltar must appoint a secretary. Both natural persons and corporate bodies are eligible to be appointed as a secretary. If a corporate body is undertaking

this function, it must ensure that it is licensed by the GFSC in order to undertake such services. In the case of a public company, the secretary must have specific knowledge and experience to discharge the functions of company secretary.

3.2 Decisions Made by Particular Bodies

The board of directors of a company is appointed to direct, control and supervise the activities and affairs of a company. Accordingly, the articles of association ordinarily empower the directors to exercise all decision-making powers of the company which are not required, by the Companies Act or by the articles of association, to be exercised by the shareholders.

The Companies Act prescribes a number of matters that are reserved to the shareholders, and that can only be passed by a shareholders' resolution. These include:

- a special resolution (as further discussed in **5.3 Shareholder Meetings**) being required to re-register a company as a public company;
- a special resolution being required to approve the terms of a proposed contract to purchase the company's own shares or to vary, revoke or renew this authority;
- a special resolution being required to make a payment out of capital for the redemption or purchase of the company's shares;
- at least an ordinary resolution (as further discussed in **5.3 Shareholder Meetings**) being required to issue, at a discount, shares in the company of a class already issued;
- a special resolution being required to authorise a reduction of the company's share capital; and
- a special resolution being required to dispense with the requirement to hold annual general meetings (as further discussed in **5.3 Shareholder Meetings**).

While the statutory requirements cannot be overridden by a company's articles of association, in some instances the Companies Act allows the company to delegate some of these matters to the board of directors under its articles of association. For example, under the Companies Act, changes to a company's articles of association must be approved by a special resolution, unless the articles of association provide otherwise.

3.3 Decision-Making Processes

Board of Directors

Board decisions are generally passed in the form of resolutions taken at board meetings. The decision-making process at board meetings is not covered by the Companies Act. The main statutory provisions relating to board meetings concern minutes of board meetings being kept and disclosure by directors of interests in contracts. Therefore, any meetings of directors are governed by the company's articles of association and by any rules made by the directors themselves by virtue of powers given to them by the articles of association. This gives companies great flexibility.

The articles of association will generally set out, among other things:

- the notice periods to be followed in respect of a directors' meeting;
- the process to be followed in cases where not all directors are physically present at the meeting; and
- the quorum and voting requirements.

In most instances, a board resolution will require a simple majority vote.

Gibraltar law does not prevent board meetings from being held anywhere in the world and allows directors to participate at board meetings

through electronic means. However, there may be tax consequences for a company in doing so.

Where a company's articles of association allow, the board of directors may also pass a resolution in the form of a written resolution without the need to convene a physical board meeting.

Shareholders

There are three types of resolutions which shareholders can validly pass.

Extraordinary resolution

An extraordinary resolution is a resolution that has been passed by a majority of not less than 75% of those shareholders who, being entitled to do so, vote in person or, where proxies are allowed, by proxy, at a general meeting of which seven days' notice has been given (unless the articles of association require otherwise), specifying the terms of the resolution and the intention to propose the resolution as an extraordinary resolution.

Special resolution

A special resolution is a resolution which has been passed by whatever majority is required for the passing of an extraordinary resolution for which not less than 21 days' notice has been given.

Ordinary resolution

An ordinary resolution is a resolution which has been passed by a simple majority at a general meeting of which seven days' notice is given (unless the articles of association require otherwise). Anything that may be done by ordinary resolution may also be done by special resolution.

Written resolutions

It should be noted that, under the Companies Act, anything that can be done by a resolution of the shareholders of a company in a general meeting can be done without a meeting by means of a written resolution signed by all the shareholders of a company, provided the articles of association allow this. However, written resolutions must be passed by the unanimous consent of shareholders, rather than the specific majority that would ordinarily be required at a general meeting.

4. Directors and Officers

4.1 Board Structure

Under the Companies Act, every company must have at least two directors, except in the case of a private company, which must have at least one director. There is no statutory maximum number of directors, although a company may make provision for a maximum number of directors within its articles of association. A sole director of a company cannot hold the position of company secretary of the same company.

There are no formal requirements or qualifications to become a director and it is possible for both natural persons and corporate bodies to be appointed as directors. There is also no legal requirement for a company to appoint a natural person as its director, so, in effect, a company can be managed and controlled by a sole director that is constituted as a body corporate. The foregoing is subject to the company not being one which is licensed, authorised, recognised or registered by the GFSC to undertake a restricted or controlled activity. The auditor of a company cannot be a director or secretary of that company.

Directors may but are not required to hold a share qualification, so it is not a requirement to hold one or more shares in order to qualify as a director.

4.2 Roles of Board Members

The Companies Act does not predefine the role for each of the board members. Typically, the board will include any number of executive directors who have management responsibilities and who perform operational and strategic business functions such as managing people and looking after business assets. One executive director can be, and usually is, nominated as chairperson. The chairperson presides over the board discussions and usually has a casting vote (unless the articles of association provide otherwise).

The board may also contain non-executive members. The non-executive director's role is to provide a creative contribution to the board by providing independent oversight and constructive challenge to the executive directors. However, it is important to note that under Gibraltar law there is no distinction between executive and non-executive directors. As a consequence, non-executive directors have the same legal duties, responsibilities and potential liabilities as their executive counterparts.

4.3 Board Composition Requirements/Recommendations

See 4.1 Board Structure.

4.4 Appointment and Removal of Directors/Officers

A company is required to file at Companies House a return in the prescribed form containing particulars specified in the register of directors and a notification of any change among its

directors, or of any of the particulars contained in the register, within 14 days from:

- the appointment of the first directors of the company; or
- a change of directors or of any of the particulars contained in the register.

Therefore, in effect, a company has 14 days from the date of its incorporation to provide Companies House with particulars of its first directors.

Subsequent directors are appointed in accordance with the company's articles of association. Under the model articles, any person willing to be appointed as a director, and permitted by law to do so, can be appointed by ordinary resolution of a general meeting or by resolution of the directors. Removal is again a matter for the company's articles of association but it would be expected that such a decision would require a resolution of a general meeting.

4.5 Rules/Requirements Concerning Independence of Directors

There are no legal requirements regarding the independence of directors under Gibraltar law. However, where a company is undertaking an activity which is deemed to be restricted or controlled under the financial services regulatory framework, and consequently regulated by the GFSC, the GFSC would expect the firm to be able to explain the basis for the number of independent non-executive directors appointed. The GFSC has established the following criteria, which should be considered when assessing the independence of individuals:

- any financial or other obligation the individual may have to the undertaking or its directors;

- whether the individual is or has been employed by the undertaking or a group entity in the past;
- whether the individual is (individually or as part of another organisation) or has been a provider of professional services to the undertaking in the recent past;
- whether the individual is or represents a significant shareholder;
- circumstances where the individual has acted as an independent non-executive director of the undertaking for extended periods;
- any additional remuneration received in addition to the director's fee, related directorships or shareholdings in the undertaking; and
- any close business or personal relationship with any of the undertaking's directors or senior employees.

Where factors are identified which could suggest threats to independence, the board should consider and discuss whether the individuals are indeed independent and document their considerations in the board minutes.

Firms should re-assess the independence of the board and the individuals on the board periodically and should document and minute how the firm has considered these issues and has applied good practice.

Conflicts of Interest

Directors are subject to a fiduciary and common law duty not to put themselves in a position where their personal interests and duty to the company conflict, unless given consent by the company, and a director must not make a profit from their position unless authorised by the company to do so.

Similarly, the Companies Act imposes a statutory duty on directors to declare the nature and

extent of any direct or indirect interest they may have in a contract or proposed contract to be entered into by the company. A director's failure to declare any interest in any contract or proposed contract to be entered into is an offence, and the director would be liable to a fine.

4.6 Legal Duties of Directors/Officers

Director and officer duties in Gibraltar are not codified under the Companies Act. Instead, they are imposed by virtue of the English common law and the equitable and fiduciary duties that were in place prior to the introduction of the UK Companies Act 2006. Broadly, these include the following duties:

- to act bona fide in the best interests of the company;
- to act for proper purposes and not act for collateral or improper purposes;
- to exercise independent judgement;
- to avoid conflicts of interest; and
- to exercise reasonable skill and care.

The Companies Act and other statutory instruments, as well as a company's memorandum and articles of association, also impose additional duties and obligations on directors. For example, the Companies Act imposes a statutory duty on directors and officers to file certain returns with the Registrar of Companies (as further discussed in **6.1 Financial Reporting** and **6.3 Companies Registry Filings**).

4.7 Responsibility/Accountability of Directors

As discussed in **4.6 Legal Duties of Directors/Officers**, directors' general duties are largely derived from equitable principles as well as common law rules. The duties of directors have therefore evolved through decisions of the courts, which have held directors to be in a fidu-

ciary relationship with the company and therefore to owe it fiduciary duties. The courts have considered directors to be in a special position of trust in relation to the company, similar to that of trustees.

While directors' duties are owed to the company, that is not to say that directors are not required to take into account the interests of anyone other than the company when discharging their duties. For instance, in order to act in the best interests of the company as a whole, directors should have regard to the interests of key stakeholders, such as employees, suppliers and customers.

Directors owe their duties to the company rather than to the shareholders, creditors or other directors of the company. A director may, however, owe duties to the creditors of the company rather than to the shareholders in an insolvency scenario.

4.8 Consequences and Enforcement of Breach of Directors' Duties

As directors' duties are owed to the company, this means that the company itself (acting through the board of directors) must take action against a director for breach of these duties, as any wrong is committed against the company itself. This principle was established in the leading case of *Foss v Harbottle* (1843) 2 Hare 461, where it was held that a wrong done to the company may be vindicated by the company alone.

The Companies Act does, however, establish an exception to this rule. See further detail in **5.4 Shareholder Claims**.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In addition to a claim for breach of duty, as previously discussed, directors may be held liable

for breaches of their statutory duties and obligations, such as those imposed under the Companies Act, the Insolvency Act and the financial services regulations (if applicable) which may, in certain instances, result in criminal penalties being imposed.

Under the previous Companies Act 1930, any provision in the articles of the company, or in any contract with the company, or otherwise, exempting any director, manager, officer or auditor of the company from, or indemnifying them against, any liability which would otherwise attach to them in respect of any negligence, default, breach of duty or breach of trust of which they may be guilty in relation to the company, was void. However, the Companies Act now clarifies that only indemnities provided by the company itself are void and further allows a company to purchase insurance for any director against any such liability.

The Companies Act also allows companies to indemnify their directors against any such liability incurred in defending any proceedings, whether civil or criminal, in which judgment is given in their favour or in which they are acquitted.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The Companies Act does not require any specific approvals in relation to a director's service contract. A director's service contract must therefore be approved in the same manner as any other commercial matter – ie, approved by the board, having regard to their duties and obligations to the company. Failing to obtain proper approval for such actions would result in the relevant appointments not taking effect.

Under the Listed Companies (Members' Rights) Regulations 2011, a listed company (that is, a company which has its registered office in Gibraltar and whose shares are admitted to trading on a regulated market situated or operating within the EU) must establish a remuneration policy as regards its directors, which must be approved at a general meeting and may only remunerate its directors in accordance with the remuneration policy.

Listed companies may derogate from the remuneration policy only in exceptional circumstances, and provided always that the policy includes procedural conditions by which such a derogation can take place and specifies the elements of the policy from which a derogation is possible.

The directors' remuneration policy is a binding policy and must be approved by the shareholders at least once every four years.

4.11 Disclosure of Payments to Directors/Officers

The Companies Act does not require the public disclosure of director remuneration.

Listed companies are required under the Listed Companies (Members' Rights) Regulations to prepare a remuneration report providing a comprehensive overview of the remuneration, including all benefits, in whatever form, awarded or due during the most recent financial year to individual directors, including to newly recruited and to former directors, and to make this report publicly available on the company's website, free of charge, for a period of ten years, beginning on the date it is first made public.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Shareholders provide some or all of the financial backing for a company. In exchange for investing in the company, a shareholder may receive a dividend and may also benefit from capital appreciation of the value of their shares. The money produced by the sale of shares enables the company to commence and continue its business.

Under Gibraltar law, a company has its own legal personality, which is separate from that of its shareholders. Shareholders will therefore only be liable for losses incurred by the company up to the value (if any) unpaid on their respective shares. It must be noted, however, that the concept of "*piercing the corporate veil*" is recognised in Gibraltar, and there may be certain instances whereby the company's separate legal identity will be set aside by the courts and the shareholders may become personally liable for the debts and liabilities of the company. For instance, courts will look behind the veil in cases of fraud or deliberate breaches of trust. In these cases, the courts ensure that an appropriate remedy is available against the individuals who have committed a wrong using a company they control.

The Companies Act establishes that the provisions of a company's constitution bind the company and its members to the same extent as if there were covenants on the part of the company and of each member to observe those provisions. Therefore, the shareholders' relationship with the company is contractual. The rights of each shareholder will depend on the rights attached to their respective shares, and this will

be set out in the company's articles of association.

In addition, shareholders may also elect to enter into a private shareholders' agreement to govern the terms on how they will behave in relation to the company. However, a shareholders' agreement is not compulsory. In addition, shareholders cannot be compelled to enter into a shareholders' agreement, and they may choose to do so only if it is in their interests. Therefore, while the articles bind all of the shareholders and the company, a shareholders' agreement would only bind the shareholders that are party to the agreement, and the usual remedies for breach of contract will be available if any of the parties commits a breach of its terms.

Shareholders' agreements may take many forms, and the need for them can arise in very different circumstances. The key benefit offered by a shareholders' agreement is that it is a private document which, in most cases, does not need to be made publicly available. A shareholders' agreement can therefore deal with private and personal matters which the shareholders prefer to keep off the public record. The articles of association, however, must be filed at Companies House and made available for public inspection. It must be noted, however, that shareholders' agreements must not include anything that fetters the company's powers to exercise its statutory duties.

Shareholders' agreements can also be useful to protect minority shareholders, as general contractual principles establish that all shareholders would need to approve a change to the agreement; whereas under the Companies Act, shareholder power is determined by a proportion of voting rights in the company.

5.2 Role of Shareholders in Company Management

Ordinarily, it is the board of directors that makes the day-to-day decisions affecting the company, and the articles of association normally govern how the directors exercise the powers of the company. The board of directors will involve the shareholders and call them to a meeting only when the need arises under the Companies Act – for example, because it is required to change the articles of association or to change the company's name.

Shareholders cannot simply overturn board decisions if they do not like the way in which the board is running the company. Instead, the shareholders have the right to appoint and remove directors from office in the articles of association. Therefore, the shareholders could remove the directors from office and replace them. In doing so, the shareholders should consider any potential employment or company law repercussions.

5.3 Shareholder Meetings

There are two types of meetings of shareholders of a company, namely:

- annual general meetings; and
- extraordinary general meetings.

On an annual basis, every company should hold a general meeting known as the company's annual general meeting, in addition to any other meetings in that year, and should specify the meeting as that in the notices calling it. Not more than 15 months should elapse between the date of one annual general meeting of a company and that of the next. However, as long as a company holds its first annual general meeting within 18 months of its incorporation, it need not

hold it in the year of its incorporation or in the following year.

A company may, by special resolution, dispense with the requirement to hold annual general meetings. Therefore, the provisions of the Companies Act requiring that a company appoint an auditor or auditors at each annual general meeting shall be deemed to have no effect in respect of that company for such time and in respect of such years as the resolution shall have effect. This does not, however, circumvent the requirement placed on a company to appoint an auditor, but rather allows it to make a single appointment, without the requirement to review the appointment on a yearly basis.

Subject to the provisions of a company's articles of association, the Companies Act establishes the provisions that have effect as to meetings and votes. These include that:

- a meeting of a company, other than a meeting for the passing of a special resolution, may be called by seven days' notice in writing;
- notice of the meeting of a company should be served on every member of the company in the manner in which notices are required to be served by the articles;
- two or more members holding not less than one tenth of the issued share capital or, if the company does not have a share capital, not less than 5% in numbers of the members of the company, may call a meeting;
- in the case of a private company, one member, and in the case of any other company, three members, personally present, shall be a quorum;
- any member elected by the members present at a meeting may be chairman; and
- in the case of a company originally having a share capital, every member shall have one

vote in respect of each share or each GBP10 of stock held by them, and in any other case every member shall have one vote.

Notice of a general meeting of a company must be given either in hardcopy form, in electronic form or by means of a website, or partly by one such means and partly by another.

5.4 Shareholder Claims

As discussed in 4.8 **Consequences and Enforcement of Breach of Directors' Duties**, directors' duties are owed to the company and not to the shareholders or any other stakeholder. Therefore, the general rule is that the company itself (acting through the board of directors) must take action against a director for breach of these duties, as any wrong is committed against the company itself.

However, in limited circumstances, the Companies Act allows shareholders to bring a derivative action on behalf of the company to enforce the company's rights and to seek relief on behalf of the company. This is an exception to the *Foss v Harbottle* rule.

Permission of a court is not needed to bring a derivative action, but it is needed to continue an action. A derivative action can be brought by a shareholder to bring a claim against another shareholder or director, for example for transactions at an undervalue and any action about which they feel aggrieved.

Derivative actions can only be brought in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default or breach of duty/trust by a director.

A shareholder can also apply to a court on the grounds that the company's affairs are being

conducted in a manner that is unfairly prejudicial to the members (or a percentage of them). Unfair prejudice claims are usually brought by minority shareholders in situations where they feel that their rights have been infringed by the majority shareholders or by the board of directors. The complaint may be based on past, present or even anticipated future events, and the court has expansive powers in this regard, including:

- the power to order the company to take or refrain from taking certain actions; and
- the power to order the company to amend its articles.

5.5 Disclosure by Shareholders in Publicly Traded Companies

There are no disclosure or other obligations on shareholders or ultimate beneficial owners in publicly traded companies.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting Annual Return

Every company is required to deliver, at least once in every calendar year, an annual return to Companies House, setting out particulars relating to the company as specified in the Companies Act. The annual return is a snapshot of certain information relating to a company, which includes:

- the name of the company;
- the company's registered number;
- the company's registered office address;
- details of the company's directors and secretary; and
- details of the company's share capital, including its shareholders.

Companies are also required to provide in their annual return details of their main activity. There is a prescribed format for the annual return, which can be found in Schedule 5 of the Companies Act.

The Companies Act establishes a separate regime in respect of the filing of annual returns by collective investment schemes. If a company notifies Companies House that it is a collective investment scheme, licensed, authorised or otherwise regulated under the FSA, then in the case of such a collective investment scheme (which is not a private fund) the annual return can omit details of shareholders and shareholding and is only required to include the amount of authorised and issued share capital, respectively. All other particulars required under the annual return would still need to be completed. An experienced investor fund, for instance, could take advantage of this exemption.

In both of the aforementioned cases, the annual return must be delivered within 30 days after the date up to which the annual return is made.

Private funds are required to deliver an annual return in the prescribed format, although they must deliver the return within six months after the date up to which the annual return is made. In addition, the Companies Act requires private funds to deliver a statement of allotments, redemptions and purchase of own shares, together with every annual return. This in turn replaces the requirement for these types of collective investment schemes to deliver a return of allotment every time they make an allotment of shares and to notify Companies House every time they make a redemption. A collective investment scheme which is not a private fund (for instance, an experienced investor fund) is neither required to complete a statement of allot-

ments, redemptions and purchase of own shares nor to inform Companies House of every occasion where it allots or redeems shares.

It should be noted that these exemptions only apply to collective investment schemes that avail themselves of the voluntary notification process to Companies House of their specific status. A collective investment scheme may choose not to make such a disclosure, and therefore to forfeit the rights to the exemptions afforded under the Companies Act.

Directors' Report and Accounts

The directors of a company are required to prepare an annual report for each financial year. Generally, this report should include the following details of the company:

- details of the company's likely future developments;
- what dividend (if any) is recommended for payment;
- a fair review of the development and performance of the business of the company (and its subsidiary undertakings, if applicable) during the financial year, as well as its position at the end of the year; and
- a description of the principal risks and uncertainties facing the company.

The Companies Act also prescribes the accounting principles to be observed in preparing the annual accounts, the layout of the balance sheet and profit and loss account, and the content of the notes to the accounts.

Companies are classified as micro, small, medium or large, and the documents to be filed at Companies House vary according to their classification, as set out below.

- Net turnover (pro-rated if more than or less than a year): micro – up to GBP632,000; small – up to GBP10.2 million; medium – up to GBP36 million; and large – over GBP36 million.
- Balance sheet total (total assets): micro – up to GBP316,000; small – up to GBP5.1 million; medium – up to GBP18 million; and large – over GBP18 million.
- Average number of persons employed: micro – up to ten; small – up to 50; medium – up to 250; and large – over 250.

A company must fall within two of the three parameters (set out above) in the financial year in question and the preceding year, in order to be classified as small, medium or large. If a company exceeds or ceases to exceed the limits of more than one of the parameters, it will continue to qualify for the relevant year unless that continues to be the case in two consecutive years. If the financial year is the company's first, the conditions only need to be met in its first financial year:

- large companies are required to file full accounts, including the balance sheet, profit and loss account, notes, directors' report and auditors' report;
- medium companies are required to file the same accounts as for large companies, except that the profit and loss account may be in an abridged format; and
- micro and small companies are required to file an abridged balance sheet only.

Accounts may be filed in a number of primary currencies (such as British pound, US dollar, euro, Japanese yen and Swiss franc).

The relevant documents must be filed within 12 months of the financial year end. Special rules

apply in the case of a company's first reporting period.

Different rules apply to companies that opt to prepare accounts in accordance with international accounting standards.

Defective accounts and directors' reports can be revised on a voluntary basis. Any revisions should be confined to the correction of those in which the previous accounts or report did not comply with the requirements of the Companies Act and the making of any consequential amendments.

6.2 Disclosure of Corporate Governance Arrangements

Under the Companies Act, "*mainstream company*" whose securities are admitted to trading on a regulated market is required to include a corporate governance statement in its annual directors' report, and that statement must be included as a specific section of the directors' report and must contain at least a reference to the following, where applicable:

- the corporate governance code to which the company is subject;
- the corporate governance code which the company may have voluntarily decided to apply; and
- all relevant information about the corporate governance practices applied beyond the requirements under Gibraltar law.

"*mainstream company*" is defined under the Companies Act as a company which is neither a public company limited by shares or by guarantee nor a private company limited by shares or by guarantee, and that is neither:

- a non-profit-making company;

- a licensed or authorised bank; nor
- a licensed insurance company.

6.3 Companies Registry Filings

In addition to the annual return and annual account filing obligations described under 6.1 Financial Reporting, companies are also required to deliver certain information to Companies House when particular changes occur within a company. Examples of event-driven filings include:

- changes to the articles of association;
- a change of company name;
- allotment of shares;
- giving, varying, revoking or renewing a director's authority to allot relevant securities;
- the making of a statutory declaration by the directors of the company to give financial assistance;
- a purchase of the company's own shares through financial assistance;
- consolidating, dividing, converting, re-classifying, subdividing, redeeming, cancelling or re-converting stock into shares;
- increasing the share capital beyond the registered capital;
- any change in any member of particulars entered in respect of any member on the register of members;
- re-denominating any of the company's share capital;
- creation of a mortgage or charge by the company;
- the acquisition of any property that is subject to a change of any kind;
- changing the registered office of the company;
- dispensing with the requirement to hold an annual general meeting;
- the passing of any special resolutions or extraordinary resolutions;

- a change among the company's directors or in any of the particulars contained in the register of directors;
- a change among the company secretaries or in any of the particulars contained in the register of secretaries;
- a change to the company's accounting reference period; and
- making a statutory declaration on the appointment of a voluntary liquidator.

The Companies Act applies various filing dates, depending on the event which triggered a filing requirement. In the majority of cases, the Act imposes a 30-day filing period. A mainstream company's accounts must be filed with Companies House once for each financial year of a company. The period allowed under the Companies Act for delivering its financial accounts is as follows:

- for a private company, 12 months after the end of the relevant financial year; and
- for a public company, ten months after the end of the relevant financial year.

Failing to comply with the accounts filing requirements before the end of the relevant period means that the company and every officer of the company who is in default is guilty of an offence and liable to pay a fixed penalty, determined as follows:

- if more than 12 months but not more than 24 months after the end of the financial period to which they relate, a fee of GBP125 will be incurred; or
- if more than 24 months after the end of the financial period to which they relate, a fee of USD175 will be incurred.

Under the provisions of the Companies Act, annual returns must also be filed within 30 days after the first or only general meeting in the year, and the company must forward to the Registrar a copy signed by a director, by the manager or by the secretary of the company. Failing to comply with such requirements means that the company and every officer of the company who is in default shall be guilty of an offence and liable on summary conviction to a fine at Level 4 on the standard scale and a daily fine at Level 3 on the standard scale.

All documents filed with Companies House are publicly available.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Unless a company qualifies as a small company (as defined under the Companies Act), the shareholders must, at each annual general meeting, appoint an auditor or auditors to hold office until the next annual general meeting.

Prior to the first annual general meeting, the first auditors of the company may be appointed by the directors at any time before that meeting, and auditors so appointed shall hold office until that meeting. The auditors may be removed by the shareholders, who may appoint a replacement auditor.

If a company qualifies as a small company and certain other conditions prescribed under the Companies Act are met, the requirements of the Companies Act relating to the appointment of auditors and the audit of accounts in respect of the applicable financial year shall not apply to that company.

A company will be classed as a small company if it meets two of the following three parameters in the financial year in question and the preceding year. If the financial year is the company's first, the conditions only need to be met in its first financial year:

- it must have an annual turnover of not more than GBP10.2 million;
- it must have a balance sheet total of not more than GBP5.1 million; and
- its average number of employees must not be more than 50.

There are requirements that govern the relationship between the company and the auditor, including that:

- an auditor shall have a right of access at all times to the books and accounts and vouchers of the company;
- an auditor shall be entitled to require from the directors and officers of the company any such information and explanation as may be necessary for the performance of the duties of the auditors; and
- an auditor of the company shall be entitled to attend any general meetings of the company at which any accounts which have been examined or reported on by them are to be laid out before the company, and to make any statement or explanation they desire with respect to the accounts.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Under the Companies Act, the directors' report must contain a description of the principal risks and uncertainties facing the company. In addition, it must also contain a description of the principal risks relating to the non-financial information discussed in **2.2 ESG Considerations** arising in connection with the company's operations and, where relevant and proportionate:

- a description of its business relationships, products and services which are likely to cause adverse impacts on those areas of risk; and
- a description of how it manages the principal risks.

INDONESIA



Law and Practice

Contributed by:

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SSEK Law Firm

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SSEK Law Firm was formed in 1992 by experienced lawyers with a vision of creating the leading independent Indonesian law firm, consistently delivering legal services of the highest international standard. Today, SSEK has more than 70 lawyers and fee earners, is one of the largest – if not the largest – independent law firms in Indonesia and is one of the most highly regarded law firms in the country. The firm's corporate governance practice has 20

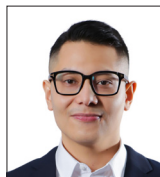
members who advise and assist corporate clients with implementing corporate governance best practices. SSEK's work includes helping corporate clients arrange general meetings of shareholders, assisting with the appointment and dismissal of members of boards of directors and commissioners, and advising on the responsibilities and liabilities of directors and commissioners.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Generally, Indonesian law acknowledges two main types of business organisation: those structured as a business entity (*badan usaha*) and those operating as a legal entity (*badan hukum*). The distinction between these two types of business organisation lies in the legal subject and liability provisions.

A business entity can take the form of a:

- civil/general partnership (*maatschap*);
- partnership; or
- limited partnership (*commanditaire vennootschap*).

A legal entity business generally takes one of the following forms:

- limited liability company;
- foundation; or
- co-operative.

The most common form of business organisation in Indonesia is a legal entity structured as a limited liability company. It is important to note

that within certain business sectors, entities are required to adopt specific organisational structures, primarily that of a limited liability company, in order to partake in the relevant business. Additionally, pursuant to Article 5, paragraph 2 of Law No 25 of 2007 regarding Investment, as last amended by Law No 6 of 2023 regarding the Stipulation of Government Regulation in Lieu of Law No 2 of 2022 regarding Job Creations as Law (the “*Job Creation Law*”) (hereinafter collectively referred to as the “*Investment Law*”), any foreign investment in Indonesia must be undertaken by means of establishing or acquiring shares in a limited liability company, unless otherwise stipulated by the relevant laws and regulations.

1.2 Sources of Corporate Governance Requirements

The primary legal framework for corporate governance in Indonesia is established in Law No 40 of 2007 regarding Limited Liability Companies, as last amended by the provisions of the Job Creations Law (the “*Company Law*”). Generally, the Company Law mandates adherence to all statutory provisions and articles of association by companies operating within Indonesia, whether they are classified as public companies or private companies.

However, specific corporate governance requirements are also stipulated for public companies, entities operating within certain sectors such as the oil and gas, banking or insurance sectors and entities designated as state-owned enterprises. For instance, the Financial Services Authority (*Otoritas Jasa Keuangan* or OJK), the regulatory body overseeing capital markets and financial sectors in Indonesia, has imposed specific corporate governance requirements on public companies and both bank and non-bank financial institutions.

In addition to the aforementioned regulations, there are various other laws and regulations pertinent to the practice of corporate governance in Indonesia that should be noted, as follows.

- Central government regulations:

- (a) Law No 8 of 1995 regarding Capital Markets, last amended by Law No 4 of 2023 regarding the Development and Strengthening of the Financial Sector (“*Law 4/2023*”) (hereinafter collectively referred to as the “*Capital Markets Law*”)
- (b) Law No 13 of 2003 regarding Manpower, last amended by the Job Creations Law (the “*Manpower Law*”)
- (c) the Investment Law; and
- (d) Law No 19 of 2003 regarding State-Owned Enterprises, last amended by Law No 1 of 2025 regarding the Third Amendment to Law No 19 of 2003 (the “*SOEs Law*”).

- OJK regulations:

- (a) OJK Regulation No 15/POJK.04/2020 of 2020 regarding the Planning and Holding of General Meetings of Shareholders of Public Companies (“*OJK Reg, 15/2020*”)
- (b) OJK Regulation No 33/POJK.04/2014 of 2014 regarding Directors and Board of Commissioners of Issuing Companies or

Public Companies (“*OJK Reg, 33/2014*”)

- (c) OJK Regulation No 21/POJK.04/2015 of 2015 regarding the Implementation of Corporate Governance Guidelines for Publicly Traded Companies (“*OJK Reg, 21/2015*”)
- (d) OJK Circular Letter No 32/SEO-JK.04/2015 of 2015 regarding Corporate Governance Guidelines for Public Companies (“*OJK CL 32/2015*”)
- (e) OJK Regulation No 45 of 2024 regarding the Development and Strengthening of Issuer and Public Companies (“*OJK Reg, 45/2024*”)
- (f) OJK Regulation No 34/POJK.04/2014 of 2014 regarding Nomination and Remuneration Committees of Issuing Companies or Public Companies;
- (g) OJK Regulation No 73/POJK.05/2016 of 2016 regarding Good Corporate Governance of Insurance Companies, as last amended by OJK Regulation No 43/POJK.05/2019 of 2019;
- (h) OJK Regulation No 48 of 2024 regarding Good Corporate Governance for Financing Institutions, Venture Capital Companies, Microfinance Institutions, and Other Finance Institutions; and
- (i) OJK Regulation No 16/POJK.04/2020 regarding the Implementation of Electronic General Meetings of Shareholders of Public Companies.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

As discussed in 1.2 Sources of Corporate Governance Requirements, specific regulations governing corporate governance requirements apply to public companies listed on the Indonesia Stock Exchange (IDX). The primary legislation

in this regard includes OJK Reg, 21/2015 and OJK CL 32/2015.

Article 1 and Article 2, paragraph 1 of OJK Reg, 21/2015 state that the OJK has the authority to issue guidelines concerning corporate governance for public companies through a circular letter, and every public company is required to implement these guidelines. To realise these provisions, the OJK has issued OJK CL 32/2015 containing corporate governance guidelines for public companies, as outlined in the annex to said letter (the “GCG Guidelines”).

OJK CL 32/2015 specifies that the GCG Guidelines therein cover five main aspects, namely:

- the relationship between public companies and their shareholders;
- the function and role of the board of commissioners (BOC);
- the function and role of the board of directors (BOD);
- the participation of stakeholders; and
- information transparency.

Although explicitly mandating that every public company adhere to the recommendations provided in the GCG Guidelines, both OJK Reg, 21/2015 and OJK CL 32/2015 adopt “*comply or explain*” approach concerning non-compliance with the GCG Guidelines. In this regard, should a public company fail to fulfil the recommendations outlined in the GCG Guidelines, the OJK will not immediately impose sanctions. Rather, the OJK will initially require the public company to explain the reason for its non-compliance and any alternative approaches taken (if any). This is evident in the obligations set forth in Articles 3 and 4 of OJK Regulation No 21/2015, where every public company is required to disclose information regarding the implementation of the

recommendations set out in the GCG Guidelines in their annual reports, which must contain at least:

- a statement regarding the implementation of the recommendations set out in the GCG Guidelines; and/or
- an explanation for any non-compliance with the recommendations set out in the GCG Guidelines, which must include at least the reasons for such non-compliance and any alternative actions taken in lieu of implementing the GCG Guidelines (if applicable).

Should the public company fail to provide such explanations, the OJK may impose administrative sanctions in the form of a reprimand letter and/or fines or take other specific actions and publicly announce the imposition of such sanctions.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

On 31 December 2024, the OJK issued OJK Reg, 45/2024. This regulation was enacted to implement the mandate under Law 4/2023 and is intended to further develop and strengthen Indonesia’s capital markets sector. OJK Reg, 45/2024 also revokes, in whole or in part, a number of existing regulations governing key aspects of the capital markets, including the registration and delisting of public companies and issuers, rights issues by public companies and the disclosure of material information or facts.

One of the key changes introduced by OJK Reg, 45/2024 relates to corporate governance, particularly in connection with the disclosure of material information or facts and the responsibilities of controllers of public companies. Under

the previous regulatory framework, public companies were required to disclose any material information or facts within two business days. Under OJK Reg, 45/2024, public companies must now disclose and report material information as soon as possible, and no later than prior to the opening of the next business day's first trading session. This accelerated disclosure timeline aims to enhance transparency and market integrity. OJK Reg, 45/2024 also asserts an obligation for public companies to identify and report their controllers to the OJK, including any subsequent changes thereto. The term "*controller*" is defined as any party that directly or indirectly owns more than 50% of the paid-up voting shares or otherwise possesses the ability to determine – either directly or indirectly and by any means – the management and/or policies of the company. The party designated as the controller is also assigned specific responsibilities, including:

- organising and attending general meetings of shareholders (GMS);
- ensuring the continuity of the public company's business; and
- appointing the members of the BOD and BOC of the public company.

Significantly, OJK Reg, 45/2024 further provides that, pursuant to a resolution of the independent shareholders in a GMS or a decision by the OJK or a competent court, a controller may be held liable for losses suffered by the company if it is proven that the controller:

- in bad faith, utilised the company for their personal interests;
- was involved in unlawful acts involving the company; or
- directly or indirectly misused the company's assets in a manner that caused the com-

pany's assets to become insufficient to satisfy its obligations.

Aside from the foregoing developments, similar to 2024, the authors have observed several developments in the environmental, social and governance (ESG) sector. One such development occurred in late 2024, when the Institute of Indonesia Chartered Accountants launched the Sustainability Disclosure Standards Roadmap, which marks a significant step in the strengthening of corporate governance in Indonesia through enhanced sustainability reporting. The roadmap was developed through stakeholder consultations and is aligned with the standards issued by the International Sustainability Standards Board. It provides guidance to ensure the creation of high-quality sustainability reports to support business activities. According to the roadmap, the use of the standards set out within it as guidance for preparing sustainability reports will become effective starting 1 January 2027, with the possibility of earlier adoption. Among other objectives, the roadmap encourages broader voluntary disclosures and a robust sustainability reporting ecosystem.

Still within the ESG sphere, the Indonesian government has expanded the SIMBARA system, a digital platform to monitor non-tax state revenue and mineral and coal trade, with the aim of enhancing transparency, accountability and regulatory compliance. In mid-2024, SIMBARA's functionality was broadened to enable the monitoring of additional key commodities, including nickel and tin. The launch and socialisation of the new features for nickel and tin monitoring were conducted in July 2024. This enhancement of the SIMBARA is expected to strengthen corporate governance practices by promoting greater oversight across the mineral and coal sector.

Finally, a notable improvement in the ESG performance of Indonesian companies occurred over the past year, as evidenced by several prestigious awards acknowledging these efforts. For example, at the Global ESG Awards in Dubai, PT Bukit Asam Tbk received multiple honours, including platinum awards for its education and awareness programme and renewable energy integration, as well as gold awards for supporting economically weaker sections and terrestrial biodiversity conservation. PT Kalimantan Prima Persada received several awards at the Global CSR & ESG Awards 2025, including the silver award for environmental excellence and the platinum award for the empowerment of women. Pertamina International Shipping was also recognised on several occasions for its dedication to women's empowerment, winning the gold award at the Global CSR & ESG Awards 2025. Other prominent companies that received recognition in the ESG sector include PT Pertamina Hulu Mahakam, Pertamina EP Zona 7, and PT PLN Indonesia Power UBP Surabaya. These awards reflect the growing commitment of Indonesian companies to advancing sustainability and promoting social responsibility.

2.2 ESG Considerations

Private Companies

For private companies in Indonesia, ESG reporting generally aligns with the requirements outlined in the Company Law and Government Regulation No 47 of 2012 concerning the Social and Environmental Responsibilities of Limited Liability Companies ("GR 47/2012"). However, it is essential to note that these requirements are relatively basic and not comprehensive. In fact, Article 74 of the Company Law specifically mandates that companies engaged in natural resource-related business activities implement sustainable economic practices to enhance the quality of life for communities and the envi-

ronment (corporate social and environmental responsibility). This suggests that only companies operating in this sector have an obligation to fulfil corporate social and environmental responsibility. There have been no significant developments in this regard.

The Company Law does not stipulate further requirements or considerations concerning the implementation of corporate social and environmental responsibility, except for requiring companies to allocate budgets for these obligations and to ensure that reports on the implementation of corporate social and environmental responsibility are included in every company's annual reports, as stipulated in Article 74, paragraph 2 and Article 66, paragraph 2 of the Company Law, respectively.

Similarly, Article 3, paragraph 1 of GR 47/2012 only mandates that companies involved in natural resources implement corporate social and environmental responsibility. There are few differences regarding corporate social and environmental responsibility requirements under the Company Law and GR 47/2012. GR 47/2012 essentially reinforces provisions previously established in the Company Law, such as:

- requiring the BOD of relevant companies to allocate funds for the implementation of corporate social and environmental responsibility in the company's annual work plan and execute corporate social and environmental responsibility as outlined in the annual work plan approved by the BOC or general meeting of shareholders (GMS), as determined in the company's articles of association (as per Article 4 of GR 47/2012); and
- ensuring that reports on the implementation of corporate social and environmental responsibility are included in the com-

pany's annual reports (as per Article 6 of GR 47/2012).

In addition to the aforementioned considerations, the OJK has mandated separate ESG reporting requirements for private companies operating as financial institutions, as regulated in OJK Regulation No 51/POJK.03/2017 concerning the Implementation of Sustainable Finance for Financial Service Institutions, Issuers, and Public Companies ("*OJK Reg, 51/2017*"), which is discussed in the following.

Public Companies

OJK Reg, 51/2017 mandates a specific ESG disclosure for public companies and financial institutions. This regulation primarily imposes the obligation for financial institutions and public companies to integrate sustainable economic practices and provide relevant disclosures to both the OJK and the public. The requirement for sustainable economic practices entails the submission of a sustainability report, either as an integral part of the annual report or as a separate document, on an annual basis.

The OJK also issued Circular Letter No 16/SEOJK.04/2021, which delineates guidelines for ESG disclosures within the annual reports of public companies. These guidelines necessitate, among other provisions, the inclusion of detailed information concerning the actions taken by companies to fulfil their social and environmental responsibilities.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The Company Law recognises three primary bodies within the corporate structure of Indo-

nesian companies: the BOD, the BOC and the GMS. Each of these principal bodies holds distinct functions and authorities.

According to the Company Law, the BOD is entrusted with managing the company in alignment with its purposes and objectives, and in the best interests of the company. In exercising its management authority, the BOD has the capacity to oversee the company's assets, enter into contracts on behalf of the company and generally represent the company both in and out of court. Despite the breadth of its management powers, the BOD operates under certain constraints, as delineated by law and/or the company's articles of association.

The BOC is tasked with supervisory and advisory functions directed towards the BOD, ensuring that the company's interests and objectives are pursued effectively. The GMS holds decision-making authority that surpasses that granted to the BOC and BOD, as stipulated by the Company Law or the company's articles of association.

3.2 Decisions Made by Particular Bodies

As briefly introduced in 3.1 **Bodies or Functions Involved in Governance and Management**, the BOD, BOC and GMS each possess distinct authorities and functions.

Given that the BOD is vested with the authority to conduct the management of the company, all decisions related to the company's management fall under the purview of the BOD. However, as previously stated, these powers may be subject to limitations as specified in the law or the company's articles of association. For example, if the BOD intends to sell or encumber company assets with a value exceeding 50% of the net assets of the company in one or more transactions, or to undertake a merger with another

company, the BOD must seek approval from the GMS.

Generally, as the BOC only has the authority to supervise and provide advice to the BOD, it does not make decisions related to the management of the company. However, there are instances where decisions of the BOC are also required for the company to undertake certain actions. For example, if during a fiscal year the company intends to distribute interim dividends to shareholders (assuming the requirements under the Company Law for such action are fulfilled), the BOD cannot proceed with this action without the approval of the BOC. Additionally, the company's articles of association may give the BOC the authority to approve specific management actions to be taken by the company.

Under the Company Law, the GMS holds authorities that the BOD and BOC are not allowed to exercise and therefore shall make various key decisions for the company. These decisions include:

- appointment of members of the BOD and BOC;
- amendments to the company's articles of association;
- payment of annual dividends;
- liquidation of the company; and
- certain corporate actions such as acquisitions, consolidations, mergers and spin-off of the company.

Similar to the BOC, the company's articles of association may grant additional authorities to the GMS to approve specific actions to be taken by the company.

3.3 Decision-Making Processes

Generally, every decision made by each body of the company is taken in accordance with the decision-making mechanism applicable to such body, as regulated in the Company Law and/or the articles of association.

However, it should be noted that the Company Law does not explicitly regulate how decisions in the BOD or the BOC for private companies are made. The Company Law does not prescribe any requirements regarding how the BOD or BOC conduct board meetings or make decisions therein. Therefore, in practice, the articles of association of each company may contain provisions regarding the conduct of board meetings and the decision-making procedures therein.

Despite the above, it should be noted that, based on Article 98, paragraph 2 of the Company Law, if the BOD consists of more than one member, then each member of the BOD has the right to act for and on behalf of the company unless otherwise specified in the articles of association. This means that specific directors may be authorised to take actions on behalf of the company without having to wait for a collective decision from the BOD, as long as they are appointed as authorised directors to represent the company. In contrast, when the BOC makes certain decisions, these decisions must be made collectively by the BOC, and no individual member of the BOC can act to represent the BOC in making decisions. This is based on the principle stated in Article 108, paragraph 4 of the Company Law, which states that if the BOC consists of more than one member, then each member of the BOC cannot act individually but must act based on decisions made by the BOC as a whole.

Unlike the provisions for the BOD and BOC, the Company Law extensively regulates how decisions can be validly made in the GMS. In short, the Company Law has established formal procedures regarding the conduct of GMS, such as how a formal GMS request is to be submitted and how the GMS invitations are to be delivered to shareholders, as well as the quorum requirements and decision-making process in the GMS. This is elaborated in **5. Shareholders**.

4. Directors and Officers

4.1 Board Structure

As indicated in the preceding sections, Indonesia, similar to other civil law jurisdictions, adopts a two-tier board system comprising the BOD and the BOC. The implementation of the two-tier board system in Indonesia is mandatory under the Company Law, meaning that every Indonesian company is required to have an active BOD and BOC functioning in the operation of the company.

Furthermore, based on Article 92, paragraph 3 of the Company Law, the BOD may consist of at least one or more members. However, Article 92, paragraph 4 of the Company Law mandates that companies engaged in activities related to the collection and/or management of public funds, companies issuing debt instruments to the public and publicly listed companies must have at least two members on the BOD. This indicates that the Company Law only stipulates the minimum number of BOD members and does not impose a maximum limit on the number of BOD members.

Similarly, Article 108, paragraphs 2 and 5 of the Company Law states that the BOC must consist of at least one member, except for companies

engaged in activities related to the collection and/or management of public funds, companies issuing debt instruments to the public, or publicly listed companies, which are required to have at least two members on the BOC.

It should be noted that the Company Law does not require that any member of the BOD or BOC be appointed as president director or president commissioner. However, the GMS may choose to make such appointments. Moreover, for the BOD, it is common for the GMS to determine the titles and authorities of each appointed member of the BOD, such as appointing one member of the BOD as the director of finance or director of operations.

4.2 Roles of Board Members

In general, the Company Law stipulates that the role of the BOD is to carry out the management of the company in compliance with applicable laws and regulations, as well as the company's articles of association.

As briefly discussed in the preceding sections, the Company Law does not differentiate the roles of different BOD members. However, in cases where there are two or more directors, the allocation of authorities and tasks among the BOD members may be determined by a resolution of the GMS. In the absence of such a resolution, the BOD may decide on this matter themselves.

As discussed in **3.3 Decision-Making Processes** and **4.1 Board Structure**, while the GMS may elect a specific member of the BOC to serve as president commissioner, it is crucial to recognise that no member of the BOC can independently carry out the duties of the BOC. According to the Company Law, this prevents variations in the roles of individual BOC members. Therefore, even if there is a president commissioner,

no decision by the BOC can be unilaterally made by the president commissioner. Instead, decisions must be made collectively by the BOC in accordance with the provisions stipulated in the company's articles of association.

4.3 Board Composition Requirements/Recommendations

As provided under the Company Law, limited liability companies in Indonesia are required to have at least one director and one commissioner. There are no stipulations regarding the maximum number of directors and commissioners. However, certain companies may be required to have more than one director and commissioner.

The requirement to have more than one director and commissioner is typically implemented by the OJK. For instance, public companies and companies carrying out financing activities are required to have at least two directors and two commissioners. Banks and insurance companies are required to have at least three directors and three commissioners.

4.4 Appointment and Removal of Directors/Officers

As a general rule, the appointment of a member of the BOD is conducted through a GMS, in accordance with Article 94, paragraph 1 of the Company Law. Directors may be appointed for a specific term and may be reappointed. Each appointment is effective on the date specified by the GMS or, in the absence of such specification, on the date the GMS is deemed closed.

Any individual may be appointed as a member of the BOD provided they have legal capacity and have not, within the previous five years:

- been declared bankrupt;

- served as a member of a BOD or BOC deemed responsible for a company's bankruptcy; or
- been criminally convicted of an offence detrimental to state finances or related to the financial sector.

Further provisions regarding the appointment, replacement and dismissal of BOD members may be outlined in the company's articles of association, subject to the minimum quorum requirements.

The procedures for the dismissal of BOD members are governed by Article 105 of the Company Law, which stipulates that BOD members may be dismissed at any time through a GMS provided there is a valid reason for such dismissal and the director concerned is given an opportunity to defend themselves, unless the director does not object to the dismissal. The dismissal becomes effective on the date the GMS is deemed closed or on a specific date determined by the GMS.

A member of the BOD may be suspended by the BOC for a specified reason as outlined in Article 106, paragraph 1 of the Company Law. During suspension, the BOD member is not authorised to perform their directorial duties. Within 30 days of the suspension, a GMS must be convened to decide whether the suspension will be lifted or if the director will be permanently dismissed.

Unless otherwise stipulated in the relevant articles of association, the GMS attendance and voting quorum for the appointment and dismissal of BOD members shall be a simple majority.

4.5 Rules/Requirements Concerning Independence of Directors

The Company Law does not recognise the concept of independent directors, and, therefore,

there is no requirement for the appointment of independent directors in Indonesian companies. This also applies to public companies, as stipulated by OJK Reg, 33/2014, which does not mandate the presence of independent directors for public companies.

However, the Company Law does acknowledge the concept of independent commissioners. Article 120 of the Company Law states that the articles of association of a company may provide for the appointment of one or more independent commissioners. Although the Company Law permits the inclusion of independent commissioners, it does not make it obligatory. In contrast, for public companies, Article 20 of OJK Reg, 33/2014 specifies that if a BOC of a public company consists of two members, one must be appointed as an independent commissioner. If the BOC has more than two members, 30% of the total members must be independent commissioners.

On the issue of conflicts of interest, Article 99 of the Company Law addresses potential conflicts by prohibiting members of the BOD from acting as legal representatives of the company if they are conflicted in such matters. This is to ensure that representation is always in the company's best interest, aligning with their fiduciary duties.

In addition to the above, Law No 5 of 1999 concerning the Prohibition of Monopolistic Practices and Unfair Business Competition, as amended by the Job Creation Law, addresses potential conflicts of interest for BOD members. It explicitly prohibits individuals from concurrently serving as directors in other companies operating in the same market or closely related business industries.

4.6 Legal Duties of Directors/Officers

As outlined in the preceding sections, Article 92, paragraph 1 of the Company Law mandates that company directors have the primary legal responsibility to manage the company in the company's best interests, ensuring that their actions are in alignment with their fiduciary duties as well as the company's purposes and objectives. Additionally, Article 98, paragraph 1 of the Company Law assigns the BOD the responsibility of representing the company in both legal and non-legal matters.

4.7 Responsibility/Accountability of Directors

The members of the BOD are entrusted to act in the best interest of the company, ensuring their actions align with the company's objectives and purposes. In fulfilling their duties, BOD members may also consider the advice provided by the BOC, provided such advice similarly aligns with the company's best interests and objectives. Ultimately, BOD members are obligated to serve solely in the best interest of the company, without consideration of the interests of other parties or bodies.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Under Article 97 of the Company Law, members of the BOD are required to perform their duties in good faith and with full responsibility. Generally, BOD members are not personally liable for company losses, provided their actions are conducted in the company's interest and in accordance with the provisions of the company's articles of association. However, BOD members may be personally liable for company losses if they are found guilty of misconduct or negligence in performing their duties. In such instances, claims can be filed against the breaching BOD members by other company organs.

If the BOD comprises two or more members, the liability is joint and several, meaning each member responsible for the misconduct or negligence is collectively liable.

On behalf of the company, shareholders representing at least one-tenth of the total shares with voting rights may file a lawsuit against BOD members in a specific district court to seek compensation for the company's losses. Additionally, members of the BOC or other BOD members also have the right to file claims on behalf of the company against any BOD member whose misconduct or negligence has caused losses to the company.

Notwithstanding the above, in the context of public companies, and as elaborated in section **2.1 Hot Topics in Corporate Governance**, Article 50 of OJK Reg, 45/2024 further stipulates that a resolution of the GMS or a decision by the OJK or a competent court may determine that a member of the BOD or BOC is personally liable for losses suffered by the public company if such losses arise due to:

- the member's bad-faith use of the company for personal gain;
- the member's involvement in unlawful acts involving the company; or
- the member's direct or indirect misuse of company assets, resulting in the company's assets becoming insufficient to meet its liabilities.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

As a principle, there is a clear separation between the personal assets and liabilities of the members of the BOD and those of the company. It is essential to determine whether a director is acting in a personal capacity or on behalf of

the company. As discussed in **4.8 Consequences and Enforcement of Breach of Directors' Duties**, personal liability of a director can be invoked if they are found guilty of misconduct or negligence in performing their duties or in other circumstances applicable to public companies.

However, a director cannot be held personally liable for company losses if:

- the loss was not caused by their fault or negligence;
- they have managed the company in good faith and with due care, in the interests of and in accordance with the company's purposes and objectives;
- they do not have a direct or indirect conflict of interest in the management actions that caused the loss; and
- they have taken actions to prevent the loss or its continuation.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

In return for their service, members of the BOD may be granted remuneration and/or other entitlements. The authority to determine the amount of such remuneration and entitlements resides with the GMS, as outlined in Article 96, paragraph 1 of the Company Law. This authority can be delegated to the BOC, in which case the BOC will make the decision through a BOC meeting.

It is important to note that the Company Law does not explicitly mandate the provision of remuneration and/or other entitlements. Consequently, the remuneration and/or other entitlements of BOD members are contingent solely upon the decision of the GMS or the BOC meeting, as applicable.

4.11 Disclosure of Payments to Directors/Officers

The Company Law provides that the remuneration payable to BOD and BOC members be included in the company's annual report, wherein the annual report shall be submitted by the BOD to the GMS after it has been reviewed by the BOC. The Company Law does not require the separate disclosure of information regarding the remuneration, fees or benefits payable to the BOD or other officers of the company to the public.

However, certain companies regulated by the OJK are obligated to make available their annual report to the public. Thus, acknowledging that the remuneration payable to BOD and BOC members must be included in the company's annual report, certain companies will inevitably be required to disclose the remuneration of BOD and BOC members to the public.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The Company Law adopts the principle of piercing the corporate veil, meaning that, similar to the BOD and BOC, there is a separation between the assets and liabilities of the company and those of its shareholders. This means shareholders cannot be held personally liable for the actions or obligations of the company. However, in the context of public companies, there are specific circumstances under which a controller may be held liable for losses suffered by the company, as outlined in section 2.1 **Hot Topics in Corporate Governance**.

As a result, shareholders do not participate in the daily management of the company. However,

due to their ownership of shares, shareholders, generally through the GMS, have significant influence over the company's affairs. This is because shareholders holding shares with voting rights can determine the appointment and dismissal of BOD members, who are responsible for the daily management of the company. Furthermore, shareholder approval is required for significant corporate actions, such as amending the company's articles of association, approving mergers and acquisitions and deciding on liquidation.

Another key variable in discussing the relationship between shareholders and the company is the distribution of dividends as a form of return on shareholders' investment. According to Article 71 of the Company Law, shareholders, through the GMS, have the authority to distribute the company's net profits, including as annual dividends. However, this article stipulates that dividends can only be distributed if the company has a positive profit balance and the mandatory reserve requirements are met for a given fiscal year. This indicates that dividends depend on the company's profitability; if the company does not generate net profits, shareholders will not receive dividends. This underscores the link between the company's financial performance and the benefits shareholders can receive from the capital they have invested in the company.

5.2 Role of Shareholders in Company Management

As previously discussed in 5.1 **Relationship Between Companies and Shareholders**, according to the Company Law, the company's BOD, not shareholders, is responsible for the management of the company. Thus, shareholders are not responsible for the day-to-day management of the company. However, shareholders, through the GMS, may influence the

company's management as they will be able to decide corporate actions taken by the company, including mergers and acquisitions, capital injection and the dissolution of the company.

5.3 Shareholder Meetings

In general, the GMS of Indonesian private companies is extensively regulated under the Company Law.

The GMS consists of an annual GMS and any other GMS that may be held at any time depending on the needs of the company. The latter is also known as an extraordinary GMS. The annual GMS must be held by no later than six months after the closing of each fiscal year. At the annual GMS, the BOD is required to submit the annual report of the company for approval, and shareholders may also ask for other items to be placed on the agenda for discussion at the annual GMS, such as the appointment or dismissal of members of the BOD or BOC, and the distribution of annual dividends.

Note that the Company Law regulates the relevant procedures and guidance for an annual and extraordinary GMS to ensure they are the same.

Procedure for GMS

Company Law provides that the BOD shall hold the GMS after a notice for such has been distributed to shareholders. The BOD can issue a notice for a GMS on its own authority or because one or more shareholders who collectively represent one-tenth or more of total shares with voting rights or the BOC has/have requested the BOD to convene a GMS.

Such request shall be submitted to the BOD by registered mail, accompanied by the reason for the request. If the BOD does not give the notice of GMS within 15 days after the date of

the request to convene the GMS is received, the following applies.

- In the case of shareholders, such shareholders may re-submit the request for the GMS to the BOC. The BOC is required to give notice of the GMS within 15 days as of the date the request to convene the GMS is received. The shareholders that request the GMS can issue the notice for GMS based on a stipulation of the chairperson of the district court with jurisdiction over the company if the BOD or BOC does not issue the notice of the GMS.
- In the case of the BOC, they may themselves give notice of the GMS to shareholders.

For a notice for a GMS to be valid, it must include the date, time, venue and agenda of the meeting, and must be accompanied by a note that the materials to be discussed in the GMS are available at the company's office as of the date of the notice of the GMS until the date the GMS is convened. Further, a notice of a GMS must be sent no later than 14 days prior to the convening thereof, excluding the date of the notice and the date of the GMS, in the form of a registered letter or through an advertisement in a newspaper.

If all shareholders attend the GMS, then the notice requirement may be waived by a shareholders' resolution passed at the GMS, in which case the GMS may be held at any time without notice.

Representation of Shareholders

The Company Law allows for shareholders to be represented in the GMS by a representative appointed by a valid power of attorney. The power of attorney must be in Indonesian, although it can be made in bilingual format if the parties deem it necessary. If executed outside Indonesia, Indonesian practice requires that the

power of attorney be executed before a notary and apostilled or legalised, as applicable, in the jurisdiction of execution.

It is important to note that a shareholder is only allowed to appoint one representative to represent them in voting for all the shares with valid voting rights owned. In other words, the appointed representative shall represent the shareholder in full. If a shareholder is represented by a member of the BOD or BOC, or by an employee of the company, the Company Law prohibits such representative to cast a vote in the GMS. Further, the Company Law stipulates that all powers of attorney must be presented to the chairperson of the GMS and that the chairperson has the right to determine the parties eligible to attend the GMS.

Chairperson of the GMS

The position of chairperson of the GMS is generally regulated in the company's articles of association. The articles of association typically provide that the president director is to act as chairperson of the GMS. In their absence, another director selected by the president director may serve as chairperson or, if none of the directors are present, a member of the BOC may be selected. If none of the directors or commissioners are present at a GMS, the shareholders may vote to select a chairperson therefor.

However, since the choice of chairperson of a GMS is not regulated in the Company Law, shareholders are free to make different arrangements for the position of chairperson in the company's articles of association.

Venue of GMS

The Company Law stipulates that the GMS must be convened in Indonesia at the domicile or place where the business activities of the com-

pany take place, as stipulated in the company's articles of association. Alternatively, the GMS may be held anywhere in Indonesia so long as all the shareholders agree and can attend.

The Company Law also allows for the GMS to be held by teleconference, videoconference or any other electronic media that enable all GMS participants to see, hear and directly participate in the meeting with each other.

Quorum of GMS

The Company Law sets out the quorum and margins of approval applicable in a GMS for various types of resolution to be adopted. Therefore, the quorum for each GMS will depend on the resolutions to be approved at that GMS. Notwithstanding the following elaboration on quorum requirements, the articles of association of a company may determine a higher (not lower) quorum and/or approval margins for the various types of meetings.

Initial GMS

For an initial GMS to discuss any matter, the Company Law provides for the following minimum quorums and margins of approval.

- Simple majority quorum – a GMS may be held to approve one of the following resolutions if it is attended or represented by shareholders who own more than one-half of the total shares with valid voting rights, and the resolution shall be valid if approved by more than one-half of the total votes cast by the shareholders in the meeting:
 - (a) annual business plan (including annual budget) (if required in the articles of association);
 - (b) appointment, replacement and termination of BOD and BOC members;
 - (c) allocation of the authorities and duties of

- the BOD;
- (d) annual report;
- (e) utilisation of net profits;
- (f) remuneration for members of the BOD and BOC;
- (g) delegation of management actions for the BOC under certain conditions for a certain period of time;
- (h) matters normally approved in an annual GMS, such as:
 - (i) a change in any method, practice or principle of accounting, except as required by changes in Indonesian generally accepted accounting principles (GAAP) determined by the company's independent certified public accountant;
 - (ii) a change to any underlying assumption, method of calculation of or depreciation of any type of asset or establishment of any material reserve;
 - (iii) the distribution or payment of any dividend or distribution in cash or in-kind of shares of capital stock of the company; or
 - (iv) the appointment of an independent certified public accountant; or
- (i) increasing or decreasing the issued and paid-up capital of the company.
- Super majority quorum – a GMS may be held to approve the following resolution if it is attended or represented by shareholders who own at least two-thirds of the total shares with valid voting rights, and the resolution shall be valid if approved by at least two-thirds of the total votes cast by the shareholders in the meeting:
 - (a) amendment to the company's articles of association.
- Absolute majority quorum – a GMS may be held to approve the following resolutions if it

is attended or represented by shareholders who own at least three-fourths of the total shares with valid voting rights, and the resolution shall be valid if approved by at least three-fourths of the total votes cast by the shareholders in the meeting:

- (a) merger, consolidation, acquisition or spin-off;
- (b) submission of court petition to have the company placed in suspension of payment obligations or declared bankrupt;
- (c) liquidation or winding up of the company;
- (d) extension of the company's term (if limited to a specific number of years); and
- (e) the sale, transfer, disposal, pledge or encumbrance of any material assets of the company that constitute more than 50% of the company's total net assets (regardless of whether in a separate or interrelated transaction).

Second and Third Meetings

Where a quorum for attendance is not reached, the Company Law permits a second GMS to be held within a maximum period of ten days and no later than 21 days after the initial GMS that preceded it took place. The notice for the second GMS must be made at the latest seven days before the second GMS is held. These requirements are also applicable for the third GMS.

The quorums and approval margins provided in the Company Law for a second and third GMS are summarised in the following.

Simple majority quorum

With respect to simple majority quorum, for the second meeting, the quorums and approval margins are as follows:

- quorum – at least one-third of outstanding voting shares; and

- approval – more than one-half of shares voted in meeting.

If the second meeting fails for lack of quorum, a third GMS may be held upon application to the district court with jurisdiction over the company, which will set the required quorum.

Super majority quorum

With respect to super majority quorum, for the second meeting, the quorums and approval margins are as follows:

- quorum – at least three-fifths of outstanding shares; and
- approval – at least two-thirds of shares voted in meeting.

If the second meeting fails for lack of quorum, a third meeting may be held upon application to the relevant district court, which will set the required quorum.

Absolute majority quorum

With respect to absolute majority quorum, for the second meeting, the quorums and approval margins are as follows:

- quorum – at least two-thirds of outstanding voting shares; and
- approval – at least three-fourths of shares voted in a meeting.

If the second meeting fails for lack of quorum, a third meeting may be held upon application to the relevant district court, which will set the required quorum.

Minutes of the GMS

The Company Law requires that minutes be made for each GMS convened. The minutes will need to be signed by the chairperson of

the GMS and one shareholder in attendance appointed by the GMS. The elucidation of the relevant article in the Company Law explains that this requirement is to ensure the accuracy of the minutes. On a separate but important note, the company may draw the minutes in the form of a deed made by a notary. In such case, the requirement for the chairperson of the GMS and a representative shareholder to sign the minutes will be waived.

Circular Resolution

The Company Law also allows the shareholders of the company to make a binding resolution outside of the GMS, provided that all of the shareholders with voting rights provide written approval by signing the relevant proposal. A resolution made outside of the GMS is commonly known as a circular resolution.

5.4 Shareholder Claims

As discussed in 4.8 **Consequences and Enforcement of Breach of Directors' Duties**, shareholders representing at least one-tenth of the total shares with voting rights may file a lawsuit against a director if the director is found guilty of misconduct or negligence in performing their duties.

Additionally, in cases where the company undertakes the following actions, and if a shareholder does not agree with such actions and incurs a loss as a result, such shareholder has the right to request the company to buy back their shares at a fair price:

- amendments to the articles of association;
- transfer or pledge of company assets valued at more than 50% of the company's net assets; or
- mergers, consolidations, acquisitions or demergers,

However, this buyback is subject to the following conditions:

- it must not result in the company's net assets becoming less than the company's total paid-up capital plus the mandatory reserves that have been set aside; and
- the total value of all shares repurchased by the company must not exceed 10% of the total paid-up capital in the company.

If this threshold is exceeded, the company must seek to have the remaining shares purchased by other parties.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Under OJK Regulation No 4 of 2024 regarding Reports on Ownership of or Any Ownership Changes in Public Company Shares and Reports on Activities of Guaranteeing Public Company Shares ("*OJK Reg, 4/2024*"), BOD and BOC members directly or indirectly owning shares with voting rights must submit a report of their ownership and any changes thereof to the OJK. Additionally, the following parties are bound by the same obligation:

- shareholders owning at least 5% of the voting shares; and
- parties who are considered controllers of public companies.

If parties subject to the aforementioned disclosure obligation see their ownership of voting shares decrease to less than 5%, they are also required to report such change to the OJK.

OJK Regulation No 4/2024 stipulates that this report must be submitted to the OJK promptly, no later than five working days from the date when such person acquires the voting shares or

from the date of any change in the ownership of such voting shares.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Pursuant to Article 66 of the Company Law, the BOD is required to submit an annual report, which has been reviewed by the BOC, to the GMS no later than six months after the end of the company's fiscal year. Among other elements, the annual report must include the company's financial statements, which should at least consist of the final balance sheet for the fiscal year in comparison with the previous fiscal year, the profit and loss statement for the relevant fiscal year, the cash flow statement and the statement of changes in equity. These financial statements must be prepared in accordance with the accounting standards set by the professional accountancy organisation recognised by the government of Indonesia.

The BOD is also required to submit the company's financial statements for audit by a public accountant if:

- the company's business activities involve collecting and/or managing public funds;
- the company issues debt securities to the public;
- the company is a public company;
- the company is a state-owned enterprise;
- the company has assets and/or annual business turnover with a minimum value of IDR50 billion; or
- the company is mandated by other regulations.

Pursuant to OJK Regulation No 14/POJK.04/2022 regarding the Submission of Periodic Financial Reports for Issuers or Public Companies, public companies are obligated to submit periodic financial statements, consisting of annual and mid-year financial statements, to the OJK and disclose the same to the public.

6.2 Disclosure of Corporate Governance Arrangements

The Company Law does not mandate companies to publicly disclose their corporate governance arrangements. However, pursuant to Article 66 of the Company Law, the BOD must ensure that the company's annual report includes, among other elements, a report on the company's activities, the names of the BOD and BOC members and a report on the supervisory duties performed by the BOC.

For further details, refer to **6.1 Financial Reporting** regarding the obligation to deliver the company's annual report.

6.3 Companies Registry Filings

In Indonesia, the Company Registry is maintained by the Directorate General of General Legal Administration (*Administrasi Hukum Umum*, or AHU) under the Ministry of Law. Essentially, the Company Registry is an official record consisting of information regarding companies in Indonesia. Among other things, it consists of information regarding a company's name, domicile, address, purpose and objectives, time period of establishment and shareholding structure. Additionally, the Company Registry contains information regarding the company's corporate documents, including the deed of establishment, articles of association and its amendments, as well as the notary in charge of creating the deed of establishment and articles of association.

Upon a company's submission of its information to the AHU, that information will be available through the AHU's website. Members of the public must pay from IDR50,000 to IDR500,000 to obtain a company profile from the Company Registry.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

As previously discussed in **6.1 Financial Reporting**, the financial statements of private companies in Indonesia generally do not require an audit by a public accountant unless the company:

- engages in business activities that involve collecting and/or managing public funds;
- issues debt securities to the public;
- is a public company;
- is a state-owned enterprise;
- has assets and/or annual business turnover with a minimum value of IDR50 billion; or
- is required to do so under other regulations.

The annual financial statements of public companies must be audited by an independent and accredited public accountant registered with the OJK.

The decision to appoint a public accountant or public accounting firm to provide audit services for the company is typically made at the GMS with a simple majority quorum.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

A company's annual report, which encapsulates its activities and performance throughout the financial year, serves as a crucial tool for the

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BOD to showcase how they manage risks and implement internal controls. While the mandatory components of the annual report as regulated under Article 66 of the Company Law may not explicitly address risk management, they indirectly highlight the BOD's approach to risk management and internal controls.

Trends and Developments

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SSEK Law Firm

SSEK Law Firm was formed in 1992 by experienced lawyers with a vision of creating the leading independent Indonesian law firm, consistently delivering legal services of the highest international standard. Today, SSEK has more than 70 lawyers and fee earners, is one of the largest – if not the largest – independent law firms in Indonesia and is one of the most highly regarded in the country. The firm's corpo-

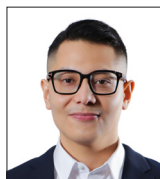
rate governance practice has 20 members who advise and assist corporate clients with implementing corporate governance best practices. SSEK's work includes helping corporate clients arrange general meetings of shareholders, assisting with the appointment and dismissal of members of boards of directors and commissioners, and advising on the responsibilities and liabilities of directors and commissioners.

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Danantara's Establishment and Accountability

At the outset of 2025, the Indonesian government advanced its national investment strategy through the establishment of a new state-owned investment entity called *Badan Pengelola Investasi Daya Anagata Nusantara*, or Danantara, modelled after Singapore's Temasek Holdings. This initiative was formalised under Law No 1 of 2025, which constitutes the Third Amendment to Law No 19 of 2003 on State-Owned Enterprises (the "SOE Law") and was approved by Parliament on 7 February 2025. The enactment reflects the government's ambition to adopt international best practices and replicate proven investment frameworks implemented in other jurisdictions.

The overarching objective of this reform is to consolidate the management of all state-owned enterprises (SOEs), their respective income streams and other state assets under a unified investment platform, thereby fostering a more robust and strategically coherent investment structure for the country.

The enactment of the amended SOE Law was swiftly followed by the issuance of Government Regulation No 10 of 2025 on the Organization

and Governance of *Badan Pengelola Investasi Daya Anagata Nusantara* ("GR 10/2025"), with both legal instruments coming into force on 24 February 2025.

As part of its establishment, Danantara is mandated to hold minimum capital of IDR1 quadrillion, which may be supplemented through further state capital injections and other lawful sources. With this capital base, Danantara can carry out direct or indirect investments and enter into partnerships with third parties. Notably, the SOE Law appears to afford Danantara a certain degree of legal immunity. While Danantara is a special legal entity controlled by the government, its profits and losses are not classified as state financial gains or losses. Furthermore, no party is permitted to seize Danantara's assets, except for the purpose of enforcing a security interest over such assets. This protection is further extended by stipulating that Danantara officials, including members of its supervisory board (*dewan pengawas*) and executive body (*badan pelaksana*), as well as its employees, are not considered state administrators (*penyelenggara negara*).

While this raises important questions regarding Danantara's financial accountability and

risk management in handling state assets and making investment decisions, it is apparent that these provisions were designed to allow Danantara greater agility in executing investments, and to shield such investments from political interference by other government institutions.

That said, the government has clarified that the Audit Board of the Republic of Indonesia (BPK RI) retains authority to examine Danantara's financial management and accountability.

Despite these developments, it is too early to assess whether the governance model adopted under the SOE Law will prove effective in practice, or whether law enforcement institutions, including the police, prosecutors, and the Corruption Eradication Commission (KPK), will interpret and apply the provisions concerning Danantara's accountability in line with the legislative intent. As such, further developments will need to be closely observed over time.

Major Reforms to the Operational Structure and Accountability of SOEs

With the enactment of the amended SOE Law, the Indonesian government has initiated significant reforms to the structure and governance of SOEs. One of the most substantial changes concerns the respective roles of the Minister of SOEs and Danantara in the oversight and management of SOEs. Under the new framework, Danantara is formally designated as the government's principal vehicle for exercising control and strategic management over all SOEs in Indonesia. Accordingly, the SOEs Law mandates the establishment of two new SOE holding entities, namely an investment holding entity and an operational holding entity, jointly established by Danantara (as a separate legal subject) and the government (represented by the Minister of SOEs). Danantara will hold a 99% ownership

stake in each of these holdings, while the state will retain a 1% equity interest in the form of golden shares, granting it special rights.

The functions of the two holding entities will differ substantially. The operational holding entity will be responsible for the day-to-day operational management of all SOEs. It is intended to serve as the holding company for all SOEs across various industries, thereby centralising operational authority under one unified platform. As a result, SOEs across Indonesia are currently undergoing extensive reorganisation to ensure that the operational holding entity becomes the majority shareholder of each sectoral holding SOE, while the state (through the Minister of SOEs) assumes a minority position with designated golden shares – either in combination with ordinary shares or as standalone instruments. It is important to note that this transformation will not affect the legal status of these enterprises as SOEs. The amended SOE Law has expanded the definition of an SOE to include not only entities in which the state owns all or a majority of shares, but also to those in which the state holds special rights through golden shares, regardless of whether it has majority or minority ownership.

Meanwhile, the investment holding entity is intended to execute asset management and investment initiatives as directed by Danantara. Unlike the operational holding entity, this investment vehicle will not be involved in the daily operational affairs of SOEs. Instead, its function is to implement strategic investment programmes using the capital allocated to it, under the purview of Danantara's broader investment agenda.

Consistent with the legal treatment of Danantara, the amended SOE Law affirms that any profit or loss incurred by an SOE is attributable solely to the SOE itself and shall not be deemed a profit

or loss of the state. In accordance with this treatment, members of the boards of directors and boards of commissioners, and employees of SOEs, are explicitly excluded from being classified as “*state administrators*”. Notably, the role of the BPK has also been significantly recalibrated. BPK RI no longer holds automatic authority to audit the financial statements of each SOE. Instead, such audits will now generally be conducted by public accountants registered with both the BPK and the Financial Services Authority (OJK) and appointed by the general meeting of shareholders of each SOE. BPK RI may only intervene in exceptional circumstances, and solely at the request of the House of Representatives (DPR). The SOE Law further stipulates that any provisions under other laws and regulations that conflict with this new regime shall be deemed inapplicable to the extent they are inconsistent. This legislative approach is rooted in the principle that SOEs are autonomous private legal entities, irrespective of whether their capital is sourced from the state budget (APBN) or from other lawful non-APBN sources.

A critical question that arises in this context is whether the newly introduced provisions will have retroactive application. The SOE Law does not expressly address this issue, leaving open the possibility that law enforcement authorities may continue to treat losses suffered by SOEs prior to the law’s enactment as state losses, potentially triggering legal consequences under the previous framework. This ambiguity underscores the ongoing need for careful observation and legal interpretation as the amended law is implemented. Achieving alignment between legislative intent and the enforcement practices of public authorities, including law enforcement and anti-corruption bodies, will be essential to ensuring legal certainty, particularly with respect

to SOE accountability and, by extension, the legal treatment of Danantara.

Inclusion of Persons with Disabilities and Women’s Participation in SOEs

The amended SOE Law introduces an explicit framework for promoting inclusivity and equal opportunity within SOEs, particularly in relation to persons with disabilities and women. It affirms that individuals with disabilities may be appointed as employees of SOEs in accordance with the prevailing laws and regulations.

Furthermore, the SOE Law expressly acknowledges that female employees are eligible to serve in key leadership roles, including as members of the board of directors, board of commissioners and other senior managerial positions within SOEs. While it is true that many inspiring women have previously held such positions even before the enactment of the amended SOE Law, the statutory affirmation reinforces the government’s commitment to gender equality and merit-based advancement. It also underscores that appointments within SOEs shall not be determined by gender, but rather by competence and qualification. As such, both men and women are entitled to equal access to career opportunities and leadership pathways within the SOE ecosystem.

Controller’s Responsibilities and Disclosure of Material Information/Facts in Public Companies

At the end of 2024, the OJK enacted OJK Regulation No 45 of 2024 concerning the Development and Strengthening of Issuers and Public Companies (“*OJK Reg, 45/2024*”). This regulation repeals, either wholly or partially, a number of previous regulations, including those governing the registration and delisting of public companies, rights issues and the disclosure of material information or facts.

One of the key developments introduced by OJK Reg, 45/2024 is a refinement in corporate governance provisions, particularly regarding the disclosure of material information and facts and the responsibilities of controllers of public companies.

Whereas the previous regime required public companies to disclose material information within two business days, the new regulation mandates that such disclosures be made as soon as possible and no later than prior to the opening of the next business day's first trading session. This expedited timeline is intended to promote greater transparency and uphold market integrity.

In addition, OJK Reg, 45/2024 reasserts the obligation of public companies to identify and report their controllers to the OJK, along with any subsequent changes thereto. The term “controller” is defined broadly to include any party that directly or indirectly owns more than 50% of the paid-up voting shares, or otherwise has the capacity, whether directly or indirectly and by any means, to determine the management and/or policies of the company. Under this regulation, the designated controllers are entrusted with broader responsibilities, including but not limited to:

- convening and attending general meetings of shareholders (GMS);
- ensuring the business continuity of the public company; and
- appointing members of the board of directors and board of commissioners.

Notably, OJK Reg, 45/2024 provides that controllers may be held personally liable for losses incurred by the company based on a resolution of independent shareholders at a GMS or a decision of the OJK or a competent court if it is proven that the controller:

- in bad faith, exploited the company for personal gain;
- committed unlawful acts involving the company; or
- misused the company's assets, either directly or indirectly, resulting in the company's inability to fulfil its obligations.

Sustainability Disclosure Standards Roadmap of the Institute of Indonesia Chartered Accountants

In addition to the developments outlined above, there has been continued progress in Indonesia's environmental, social and governance (ESG) landscape. Notably, towards the end of 2024, the Institute of Indonesia Chartered Accountants introduced the Sustainability Disclosure Standards Roadmap. This initiative represents a major advancement in strengthening corporate governance through improved sustainability reporting practices. Developed through extensive stakeholder engagement and aligned with the standards issued by the International Sustainability Standards Board, the roadmap provides detailed guidance aimed at facilitating the preparation of high-quality sustainability reports to support business operations. The roadmap indicates that the standards are to be adopted as a reference for sustainability reporting starting from 1 January 2027, although an earlier adoption date is encouraged.

Among other key points, the roadmap promotes broader voluntary disclosures and the development of a robust sustainability reporting ecosystem. This includes the development of relevant standards for preparing and assuring sustainability reports, with a particular focus on tailoring these standards to the varying sizes and capacities of businesses. While the roadmap aligns with the International Sustainability Standards Board guidelines, it also calls for the creation of simpler

standards to accommodate smaller businesses, including micro, small, and medium enterprises. Furthermore, it emphasises the necessity of regulatory updates, and the qualifications of the professionals involved in the reporting and auditing processes. To ensure the effectiveness of these initiatives, the roadmap also stresses the importance of enhancing the capacities of both the individuals and institutions involved in the preparation, assurance and oversight of sustainability reports.

The Expansion of the SIMBARA Tracking System

Still within the ESG sphere, the Indonesian government has taken steps to enhance transparency and accountability in the mineral and coal sector by expanding the capabilities of the SIMBARA platform. Preliminarily, SIMBARA is a digital platform designed to monitor non-tax state revenues and track mineral and coal trading activities. Several key issues prompted the introduction of SIMBARA, including discrepancies in mineral and coal data between the upstream and downstream sectors, inadequate oversight of mineral and coal sales and transportation, and the lack of an integrated system for coal services and supervision.

In mid-2024, the government announced updates to the SIMBARA system aimed at improving the monitoring of the mineral and coal sector. The new features include enhanced tracking of mineral and coal production, real-time monitoring of export and domestic trade transactions and integration with licensing and customs systems. Since the launch of SIMBARA, the government has been able to detect various forms of fraudulent activity. As such, the continued enhancement of the SIMBARA system reflects the government's broader commitment to strengthening governance, increasing transparency, preventing fraud, and supporting sustainable resource management practices in Indonesia.

Indonesian Companies Recognised for ESG Efforts

The authors have also seen an increase in the ESG performance of Indonesian companies, as reflected in several prestigious awards recognising their contributions. Domestically, several publicly listed companies were recognised as recipients of the ESG Award 2024, organised by *Yayasan Keanekaragaman Hayati Indonesia* (KEHATI). These companies include PT Bank Mandiri (Persero) Tbk, PT Bank Rakyat Indonesia (Persero) Tbk, PT Avia Avian Tbk and PT Sarana Multi Infrastruktur (Persero). PT BNP Paribas Asset Management, *PT Samuel Aset Manajemen*, PT Xurya Daya Indonesia, *PT Sosial Bisnis Indonesia* and *PT Khazanah Hijau Indonesia* were also named as recipients of the ESG Award 2024 by KEHATI.

At the international level, PT Bukit Asam Tbk received multiple awards at the Global ESG Awards in Dubai, including platinum awards for its education and awareness programme and renewable energy integration, and gold awards for supporting economically weaker sections and for its efforts in terrestrial biodiversity conservation. PT Kalimantan Prima Persada earned multiple recognitions at the Global CSR & ESG Awards 2025, including a silver award for environmental excellence and a platinum award for the empowerment of women. Pertamina International Shipping received multiple recognitions for its commitment to women's empowerment, including a gold award at the Global CSR & ESG Awards 2025. Other notable companies to receive awards in the ESG sector include PT Pertamina Hulu Mahakam, Pertamina EP Zona 7 and PT PLN Indonesia Power UBP Surabaya. These recognitions highlight the growing commitment of Indonesian companies to advancing sustainable practices and promoting social responsibility.

IRAQ

Law and Practice

Contributed by:

Ahmed Al-Janabi and Sarmad Akrawi

MENA Associates in association with AMERELLER



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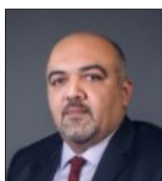
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MENA Associates in association with AMERELLER is a leading international law firm largely located in the Middle East. It has more than 60 lawyers working in fully integrated offices in Basra, Baghdad, Berlin, Cairo, Dubai, Erbil, Munich, Ras Al Khaimah and Tripoli. The offices are legally separate entities, as required by applicable laws, but managed and operated as a single law firm. Its Baghdad office was established in 2003 and is a full-service office, advising local and international corporate clients, government authorities and NGOs in all areas of commercial and corporate law, including

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Non-public companies in Iraq are established in accordance with the Companies Law No (21) of 1997, as amended by Law No (17) of 2019 ("*Companies Law*"). The Companies Law recognises two types of companies:

- private companies, in which public sector participation, if any, is limited to 25% of share capital; and
- mixed companies, in which private persons and public entities jointly establish an entity with at least 25% public sector participation.

Private companies may take the form of a limited liability company (LLC), joint stock company (JSC), general partnership, individual enterprise or simple company. Mixed companies may only take the form of LLCs or JSCs.

The entities most commonly registered by persons conducting business in Iraq are limited liability companies and branches of foreign companies.

The Companies Law now requires LLCs and JSCs to hold at least 51% Iraqi shareholding capital (by Iraqi individuals or corporations). It should be noted that the Companies Law as amended does not apply to the Kurdistan Region of Iraq (KRI), as to date it has not been passed by the Kurdish Parliament. As a result, 100% foreign participation is permissible in the KRI.

The Iraqi Constitution provides the Kurdish Parliament with legislative powers, with the exception of certain matters that are reserved to the federal government. As far as the Kurdish legislature has not made use of the legislative competencies conferred on it, Iraqi federal law applies if it has been either adopted by the Kurdish legislature or enacted prior to 1992.

On the other hand, the Kurdistan regional government has its own ministries and authorities that mirror those of the federal government; however, they operate independently of the federal authorities. This results in the need to register an entity in parallel in the KRI and in Baghdad.

Unless otherwise expressly indicated, references to any law, instruction or regulation is a reference to such a statute as applied in Federal Iraq.

Limited Liability Company

An LLC may be established by a maximum of 25 shareholders. There is no minimum requirement. The shareholders may be legal entities or individuals, or a combination of both.

The general assembly of shareholders appoints and determines the powers of the managing director, who may be a foreign national.

The minimum capital for an LLC is IQD1 million. Any public subscription of shares in an LLC is prohibited.

Joint Stock Company

A mixed or private JSC is founded by at least five shareholders, and their liability is limited to the amount payable on their shares.

The general assembly of shareholders elects the board of members which governs the JSC. The board of a private JSC is composed of a minimum of five and a maximum of nine members. The board of members then elects the chairman and deputy chairman from among its members. The liability of the board of directors is the same as that of the managing director of an LLC.

The minimum share capital of a JSC is IQD2 million. Unlike an LLC, part of the shares of a JSC must be offered to the public for subscription. The public subscription must be completed before a certificate of establishment can be issued.

Insurance and financial investment companies are required to register as JSCs.

Other possible entities under the Companies Law include the following.

- **General Partnership:** A general partnership is an association of two or more persons who are jointly and severally liable for partnership debts. The minimum capital requirement is IQD50,000.
- **Individual Enterprise:** An individual enterprise consists of one natural person who owns the single share and is personally liable for the enterprise's debts to the full extent of his personal assets.
- **Simple Company:** A simple company is established by a minimum of two and maximum of five partners. The partners may also contribute to capital through services. The establishment process is, as the name suggests, extremely simple.
- **Holding Company:** The holding company may be in the form of a JSC or LLC, and has control over one or more JSCs or LLCs. The holding company was introduced as a permissible type of company under the newly amended Companies Law.

Branch of a Foreign Company

A common registered entity is the branch of a foreign company. It should be noted that the commercial activity of the branch is limited to the registered activity of the foreign company. The foreign company would also be liable for any liabilities of the branch. The registration requirements for branches in Iraq are stipulated in Regulations No (2) of 2017 on Foreign Companies' Branches.

For the registration of a branch in Federal Iraq, the foreign company must have been established at least two years earlier. Any managerial changes must be approved through a shareholders' resolution by the parent company.

1.2 Sources of Corporate Governance Requirements

The main source of law related to corporate governance requirements in Iraq is the Companies Law. No code or regulation has to date been enacted specifically to regulate corporate governance matters.

The Companies Law sets out most of the corporate governance rules, determining managerial powers and responsibilities of the different bodies within the company.

The articles of association may also set out rules and requirements, though this is not particularly mentioned in the law. However, the document must at a minimum include the following:

- name and form of the company;
- the company's objects and type of business;
- address of head office in Iraq;
- name, nationality and profession of founder(s);
- share capital, amount of cash and in-kind contributions, a description of any contributions in kind, and names of the contributors; and
- number of elected members on the board of directors (in a JSC).

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Joint-stock companies are the only type of entity in Iraq whose shares may be publicly traded. It is required for a part of the shares to be offered for public subscription.

The chairman or deputy chairman may not also be the managing director of the JSC.

The following committees are to be established comprising members selected from the board of directors:

- audit committee to recommend external, independent auditors; and
- compensation committee to determine the remuneration of board members and the managing director.

Committee members may not be officers, employees or holders of 10% or more of shares in the company.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

There are no other key corporate governance rules and requirements to be drawn out in Iraq.

2.2 ESG Considerations

There are no laws or regulations for companies regarding environmental, social and governance (ESG) issues. These provisions may be provided for in the company's internal policies or articles of association based on standard international practices in this area.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The general assembly of shareholders consists of all members of the company and is considered the highest authority of the company, according to the Companies Law.

The general assembly of an LLC appoints and determines the authorities of the managing director and deputy managing director. The deputy

managing director may carry out the managing director's responsibilities in the latter's absence. A managing director's functions involve carrying out the day-to-day business operations of the LLC.

Private JSCs are governed by a board of directors consisting of a minimum of five and a maximum of nine members elected by the general assembly.

Being a member of the board of directors is subject to the following eligibility requirements:

- they must be legally qualified and not banned from managing a company under law or legal decision; and
- they must own no fewer than 1,000 shares – any number below this must be increased to meet the minimum within 30 days of membership.

The board must elect the chairman and deputy chairman from among its members. The managing director is not required to be a board member. However, the managing director may not also be the chairman, and cannot be the managing director of any other joint stock company.

The powers of the board of directors are determined by the Companies Law and mentioned in **3.2 Decisions Made by Particular Bodies.**

3.2 Decisions Made by Particular Bodies Shareholders

As the governing body of the LLC, the general assembly of shareholders may deal with any matter that is in the company's interest. The shareholders appoint, remove and determine wages and powers of the managing director and must also approve the LLC's budget, final accounts and annual plan.

Managing Director

Under the Companies Law, the responsibilities of the managing director in an LLC are the same as that of the board of directors of the joint stock company, subject to the decisions of the general assembly.

The managing director must carry out the tasks within the powers assigned by the general assembly (or board of directors in the JSC).

Board of Directors

In a JSC, the board of directors must meet at least once every two months at the request of the chairman or any one of its members. The board is responsible for the necessary administrative, financial, planning, organisational and technical duties of the company's business, except those which fall under the powers of the general assembly. In particular, the board of directors has the following powers:

- appointing the managing director and determining his/her remunerations and authorities;
- dismissing the managing director;
- implementing the general assembly's decisions and follow-up thereof;
- evaluating an annual plan for the company's activities as prepared by the managing director;
- preparing final accounts of the previous year, to be reported to the general assembly along with the results of the annual plan;
- following up on implementation of the annual plan with periodic reports to the auditor;
- preparing statistical studies to further develop the company's business;
- making decisions related to loans, mortgages and securities;
- establishing an audit committee within its board to recommend external, independent auditors; the audit committee is responsible

for meeting the auditors and ensuring the accuracy of their work; and

- establishing a compensation committee from its board to recommend the compensations for the board and managing director; these committee members must be impartial and may not be employees or own 10% or more of the company's shares.

The chairman must sign any decision made by the board of directors and follow up on the implementation of such decisions.

3.3 Decision-Making Processes The Shareholders (General Assembly)

The general assembly of shareholders makes decisions through meetings, which are required to be held twice a year, or once a year in the case of a joint stock company. The details of the meeting process are found in **5.3 Shareholder Meetings**.

The Board of Directors

The board of directors must meet seven days after the formation of a company and shall elect the chairman and deputy chairman for a one-year term that is renewable.

The board of directors is required to meet at least once every two months at the invitation of the chairman or any of its other members. The meeting should be held at the company's head office or as determined by the chairman if the head office is not an option at that time.

Board decisions are reached through an absolute majority of the votes. In the case of a tie, the chairman's vote prevails.

4. Directors and Officers

4.1 Board Structure

The board of directors is composed of between five and nine members elected by the general assembly. The membership lasts three years and is renewable. The board of directors appoints a chairman and deputy chairman.

In a mixed JSC, the board of directors consists of seven members, two of whom represent the public sector and five of whom are elected by the general assembly. The composition would be three and four members respectively if the public sector's share capital exceeds 50%.

4.2 Roles of Board Members Board Members

The board members appoint and dismiss the managing directors, carry out the general assembly decisions, prepare final accounts, and handle the administrative, financial, planning, organisational and technical duties of the company, as stated in the Companies Law.

Chairman

The chairman is required to follow up on the implementation of the decisions made by the board of directors. The chairman's vote determines the result of the board decisions whenever there is a tie.

Deputy Chairman

The deputy chairman, also appointed by the board of directors, shall replace the chairman in his absence. The deputy chairman may not become the managing director.

4.3 Board Composition Requirements/ Recommendations

There must be between five and nine members of the board of directors in a private JSC. Each

board member must own at least 1,000 shares in the company. The board members may be freely determined by the shareholders, as long as they are legally qualified under the applicable laws.

4.4 Appointment and Removal of Directors/Officers LLC

The managing director and deputy managing director of an LLC are appointed by the general assembly and may only be removed by the general assembly.

The LLC must also have one auditor and one legal adviser, who must be Iraqi nationals. These officers are also appointed and dismissed by the general assembly.

JSC

The general assembly may elect or dismiss a chairman or board member through a secret ballot held during its meeting. The chairman or deputy may also be considered as having resigned if they fail to attend three consecutive meetings or successive meetings for over six months and without a legitimate reason.

The board of directors appoints a managing director and has the power to remove him/her through a decision. The decision must cite the reasons for removing the managing director and should be signed by the chairman. The same steps apply for the appointment and removal of a deputy managing director.

There are no restrictions on who may be appointed as managing director of a company.

4.5 Rules/Requirements Concerning Independence of Directors

The Companies Law states that the chairman or board members cannot have any direct or

indirect interest in any business or transaction undertaken by the company, except where the general assembly grants approval after being made aware of the nature and extent of the interests. The chairman or board member will be directly liable for any damage that may arise in violation of that rule.

Voting on a matter in which the chairman or board member has direct or indirect interests is also prohibited unless a majority of the members grant permission after the nature and extent of the interests are disclosed.

4.6 Legal Duties of Directors/Officers

The Companies Law provides that the chairman and members of the board of directors shall do their best to serve the company's interests and run the company in a sound and legal manner. They are liable to the general assembly in carrying out these duties.

They must also disclose any direct or indirect interests they have with regard to any transactions and dealings with the company.

4.7 Responsibility/Accountability of Directors

Directors are responsible before the general assembly in carrying out their duties. They are required to serve the interests of the company as they would their own personal interests.

4.8 Consequences and Enforcement of Breach of Directors' Duties

An inspection may be requested by a shareholder of more than 10% of share capital, the managing director of a company, or a member of the board of directors in the case of a JSC, if there are reasonable grounds to believe that there is a violation of law, shareholders' resolution or the company's articles of association.

The inspectors will be determined by the Registrar of Companies (“Registrar”), who would then inform the relevant authorities so that action may be taken if there is a breach of duties by a director or manager. The Registrar would also guide the company based on the findings of the report.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Directors or officers shall be held liable if the duties mentioned in 4.6 **Legal Duties of Directors/Officers** are proven to be violated.

The liability of LLC shareholders towards third parties is limited to the nominal value of their shareholding. However, Iraqi courts have yet to develop a consistent doctrine concerning the liability of shareholders and/or managers towards third parties.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

All payments to current or previous board members or managing directors must be included in a detailed report on the final accounts to be submitted to the shareholders.

The shareholders determine the remuneration of the managing director of an LLC.

In a JSC, the general assembly of shareholders fixes the remuneration of the chairman, deputy chairman and other members of the board of directors, which must be in proportion to the latter’s scope of work and fulfilment of the company’s plans and profits. The board of directors determines the remuneration of the managing director.

Although the consequence is not specified in the law for non-compliance with the approval

requirements, inspections may be carried out by the Registrar, who must inform the responsible authorities of any questionable findings in their report in order for the appropriate action to be taken. This could lead to suspension of the company’s file at the Registrar and possible fines.

4.11 Disclosure of Payments to Directors/Officers

No public disclosures with regard to remuneration, fees or benefits to directors or officers are required to be made.

As mentioned previously, the final accounts report disclosed to the shareholders must include the payments received by board members or the managing director in cash or in kind.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The Companies Law governs the relationship between the company and its shareholders.

Shareholders may not use their powers and voting rights for their own personal gain and make decisions which harm or put the company at a disadvantage. Furthermore, they may not withdraw capital or transfer assets if prohibited or if insolvency is imminent.

Shareholders of over 10% of the shares of a company may propose items to be included in the agenda of the general assembly meeting, which must then be passed by the majority of shareholders present there.

The general assembly of shareholders has the following powers in the company:

- fixing remuneration of chairman and board members;
- discussing and approving the report of the founder/s regarding establishment procedures;
- electing and dismissing representatives of shareholders within the board of directors;
- making decisions on reports from the board of directors or managing director, as well as the auditor;
- discussing and approving final accounts;
- discussing and approving the proposed annual plan and budget (not applicable to JSCs);
- appointing and fixing remuneration of the auditor (not applicable to JSCs);
- making decisions on proposals regarding loans, mortgages and securities (for LLCs);
- approving the percentage of profits to distribute among members; and
- approving employment rules in the case of a mixed joint-stock company.

5.2 Role of Shareholders in Company Management

According to the Companies Law, the general assembly of shareholders is the governing body of the company. It is the body which elects and dismisses representatives of shareholders in the board of directors.

The general assembly of shareholders also makes decisions on the reports from the managing director of the company or board of directors of a JSC, as well as the auditor's reports. It is also authorised to appoint and determine the wages of an auditor, and approve the company's final accounts, proposed annual plan and budget, except in the case of a JSC. Other matters include decisions on borrowing. In the JSC, the shareholders determine the wages of the board

of directors, including the chairman and deputy chairman.

5.3 Shareholder Meetings

Iraqi law does not distinguish between ordinary and extraordinary shareholders' meetings.

The general assembly is required to hold two meetings a year, or once a year if it is a joint stock company, by invitation of the founder(s) of the company (for the constituent meeting held within 30 days of the issuance of the company's certificate of establishment), chairman of the joint stock company or managing director in other companies, or at the request of members of the company who own at least 10% of the paid-up capital. The meeting may also be called upon by the Registrar or the auditor.

General assembly resolutions are passed through a simple majority of votes. Votes may be made in person or by proxy. A proxy may be issued to another shareholder or a third party, and must be deposited with the company three days prior to the meeting. Resolutions may not be passed unless a majority of the members are present.

In an LLC, the general assembly may determine appointments, wages and managerial authority, as well as approve budgets and annual plans. In the JSC, the general assembly elects and determines the wages of the board of directors.

Decisions by the general assembly are to be kept in a special register and signed by the chairman.

The company administration should inform members of their invitation to the meeting or send it to their postal addresses. In a JSC, the invitation to a meeting must be issued in the

Registrar's bulletin, two daily newspapers and the Baghdad Stock Exchange.

5.4 Shareholder Claims

Shareholders who hold at least 10% of the share capital may request inspection of the company if there are reasonable grounds to believe that the company has violated a provision of the Companies Law, the company's articles of association, or a resolution passed by the general assembly.

Shareholders who hold at least 5% of the shares may object to a resolution of the general assembly by petition to the Registrar within seven days of the resolution being passed.

5.5 Disclosure by Shareholders in Publicly Traded Companies

The Registrar must be provided with all data in relation to the subscription process, the names of subscribers and number of shares, and amounts paid against the value of shares.

There are no specific obligations in relation to the ultimate beneficial owner of publicly traded companies. The owner of record is the legal owner as far as the authorities are concerned.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

The managing director of a company is required to prepare the final accounts within the first six months of each year, write a detailed report on them, and submit them all to the general assembly. In a JSC, the board of directors is responsible for this. The board must also submit periodic reports to the auditor and an annual report to the general assembly regarding the results of the implementation of the annual plan.

The final accounts would also be audited by external auditors appointed by the general assembly. The auditors will provide a report to the company that addresses their findings and the extent of the accounts' compliance with the law and the company's articles of association.

Copies of the final accounts and the related reports must be submitted to the Registrar.

6.2 Disclosure of Corporate Governance Arrangements

Companies are required to submit a UBO form to the authorities, disclosing the shareholders, board members and manager of the company.

6.3 Companies Registry Filings

The general assembly meeting notes and decisions should be recorded in the minutes of the meeting and sent to the Registrar within four days of being implemented. Copies of the final accounts, annual plan and related reports must also be sent to the Registrar.

General assembly meetings regarding the final accounts must be notified to the Registrar, and the following must be sent:

- the annual list;
- the final accounts of the previous year and the auditor's report; and
- the managing director's or board of directors' report on the annual plan of the previous year.

The Registrar is entitled to obtain any document from the company for the purpose of carrying out its responsibilities under law.

Companies are now required to present evidence of an Iraqi top-level domain (.iq) and an Iraqi Post Office Box (PO Box) filed by the com-

pany. This is required for all companies registered in Federal Iraq.

None of the filings made with or sent to the Registrar are made publicly available.

The company may be subject to inspection by the Registrar for any violation of the aforementioned. Any questionable findings will be reported to the responsible authorities in order for the appropriate action to be taken and will lead to suspension of the company's file and payment of fines. If the Registrar is prevented from seeing the company's records or documents, the company official responsible for this action shall be, according to the Companies Law, subject to imprisonment for up to six months or a fine of up to IQD12 million.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

External auditors are appointed by the general assembly and are required to evaluate a company's final accounts based on the law and the company's articles of association, and should apply international accounting standards.

In a JSC, external auditors are selected by the audit committee established by the board of directors. The external auditors meet with the audit committee and apply international accounting standards in their work. They may be subject to questions regarding the accuracy and correctness of their reports.

In a mixed company, the accounts are required to be audited by the Financial Control Bureau.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The board of directors of a JSC is required to establish an audit committee within the board that will recommend external, independent auditors. These members may not be officers or employees of the company, or hold 10% or more of its shares.

The board of directors of a JSC, or managing director in the case of other companies, must also prepare a report in relation to the final accounts that includes details on the company's activities, such as any transaction in which major shareholders, board members or the directors have a direct or indirect interest.

The chairman of a JSC, or managing director in the case of other companies, must sign the company's final accounts and shall be liable for the correctness of the statements.

Trends and Developments

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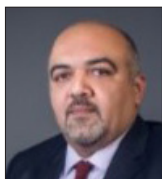
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and corporate law, including general corporate governance issues, director duties and obligations, and corporate housekeeping. The offices in Baghdad and Erbil are each staffed with teams of seven locally admitted lawyers. The firm has advised major international companies and organisations on their entry strategy to Iraq, and continues to provide legal and strategic advice on major investments including infrastructure projects, project financing, direct investments, real estate, M&A, general commercial transactions and day-to-day legal matters.

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Developments in Corporate Governance in Iraq

Over the past year, there have been numerous developments at the corporate level, most of which have concerned the requirements and filing procedures with various ministries and government offices, chiefly the Registrar of Companies (RoC) and the Ministry of Labour and Social Affairs (MoLSA).

Regarding the filing process, both the RoC and MoLSA have introduced new filing systems as part of the broader governmental initiative to digitalise the public sector. These portals, however, are somewhat outdated and still rely on manual review rather than automated electronic verification systems. Despite this, all companies are now required to initiate registration through the online portal and maintain an account in order to carry out any filings or related actions. While certain services must still be accessed via in-person applications, the long-term goal remains the full digitalisation of the process.

Official fee payments have also been shifted to an electronic format. However, this transition has been anything but smooth, hampered by many technical issues and the general reluctance of

the public to move away from cash payments. One of the most significant obstacles is the maximum limit on designated debit cards, which, in some instances, falls short of the required amount for payment.

As for the filing itself, the process remains far from truly digital. In most cases, it involves merely scanning and uploading documents for officials to review manually. Often, the originals are still requested before the filing can be finalised. Consequently, some argue that this system has actually introduced more delays and complications, rather than streamlining or accelerating the filing process.

With regard to the new corporate filing requirements, a number of additional obligations have been introduced, primarily by the RoC. These include:

- UBO forms;
- PO box registration;
- local domain registration;
- good standing letter from the tax office; and
- good standing letter from MoLSA.

The rationale behind the registration of some of these documents remains unclear, particularly in the case of the PO box and locally registered domain. The domain registration process is proving increasingly problematic, as fees for well-known companies can be extremely high – reaching up to USD6,000 annually. Moreover, there is concern that domains using protected, well-known names could be granted to any company that pays the fee first.

In contrast, the UBO requirement and good standing letters are more justifiable, as they aim to ensure that companies are in compliance with all applicable laws and regulations in Iraq. While obtaining these documents is theoretically straightforward, in practice it has become a lengthy and difficult process, largely due to understaffed government offices. The UBO forms pose a different challenge, as they are frequently rejected by authorities in parent countries, and legalisation of the documents has become increasingly difficult.

A more recent development concerns access to the RoC itself. Lawyers and authorised representatives of companies must now book an appointment a day in advance for any in-person visit. This system has also proven problematic, as the number of available daily slots is limited. Booking opens only twice a day and is often fully booked within minutes, making it difficult to secure a time.

In summary, while the overarching aim of these reforms is to transition into a digital framework and accelerate administrative processes, the lack of thorough research and inadequate preparation for implementation have resulted in further delays. In some cases, the cumulative effect of these poorly executed changes has brought

companies to a standstill, hindering their ability to operate effectively in Iraq.

Further developments

Other legislative developments in Iraq include proposals aimed at facilitating investment processes. Iraq recently acceded to the New York Convention, offering foreign investors assurance that disputes can be resolved and enforced against Iraqi entities. Additionally, Iraq has signed several bilateral investment and double tax treaties, including with Turkey, Saudi Arabia, and the UAE, although these treaties are yet to be ratified by Parliament. The housing fund law is also under review to make financing more accessible for Iraqis purchasing housing in new residential compounds.

The housing sector is experiencing a surge of investment in Iraq. The government continues to implement regulatory reforms aimed at improving the business environment and attracting foreign investment. Housing needs are being addressed through major investment projects. Earlier this year, the Iraqi government signed a major contract with Naguib Sawiris' Orascom Investment Holding for Iraq's largest residential project to date, set to include 120,000 housing units in Baghdad. Additionally, the government has initiated several large construction projects to address inadequate infrastructure, worsened by an influx of migrants from rural areas due to economic challenges and climate-related issues like water shortages. Local and foreign developers are being offered contracts for new city projects in Baghdad, Karbala, Babylon, Al-Anbar, and Nineveh governorates, which will feature housing units, schools, commercial centres, healthcare facilities, and other amenities.

Large-scale real estate development creates investment opportunities in many sectors,

although they face similar challenges in navigating Iraq's bureaucratic business environment. Despite the Iraqi Investment Code No 13 of 2006's provision of a one-stop shop at the National Investment Commission for all licensing needs, investors still need to obtain licences and authorisations from each individual ministry, delaying operations for several months to over a year.

De-dollarisation policy

The Iraqi government's "*de-dollarisation*" policy is still continuing, and has now been coupled with a broader move towards mandating electronic payments in nearly all aspects of official transactions, as well as a significant portion of the private sector. For the past two decades, the US dollar has been widely accepted in Iraq for commercial dealings and investment activities. However, in 2023, the government and the Central Bank of Iraq introduced stringent restrictions on the use of the US dollar in an effort to boost confidence in the Iraqi dinar. These measures included strict conditions for foreign currency transfers and repatriation of profits, leading to a shortage of dollars and a gap between the official exchange rate and parallel market rates.

Recent requirements by the Companies Registrar, as mentioned above, were based on the Federal Budget Law for 2023, 2024, and 2025. These require companies to register an Iraqi website with an Iraqi top-level (.iq) domain and lease an Iraqi PO Box within a 60-day grace period starting from 16 January 2024. Non-compliance will result in the suspension of corporate files until these requirements are met, adding more obstacles to the licensing process despite government efforts to streamline it.

Although the government has previously proposed laws and regulations aimed at digitalising

the company registration process, these proposals have yet to be enacted into law. Nevertheless, certain regulations, as mentioned above, have been put in place to initiate digitalisation efforts, including streamlining government procedures, including tax and customs processes, and enacting an access to information law.

Meanwhile, discussions are ongoing regarding the repeal of the 2019 law that amended the Iraqi Companies Law, which currently caps foreign ownership of federal Iraqi companies at 49%. However, the current momentum suggests an amendment to this law is more likely, reducing the local shareholding requirement to just 30% of the shares, down from 51%. Presently, foreign investors typically need an Iraqi partner or must devise alternative corporate governance strategies to retain control over their businesses.

Conclusion

While the Iraqi government aims to attract more foreign investment and has initiated infrastructure development, the implementation of legislative reforms to streamline processes remains crucial. The construction sector and other attractive sectors will continue to offer opportunities and challenges for investors. Corruption and security risks persist, hindering investment along with the delay in the implementation of the new developments due to the lack of a wide vision and understaffed offices. Real estate remains a significant sector for money laundering. The opaque Iraqi bureaucracy presents challenges and hampers business opportunities. Mitigating these risks requires a nuanced understanding of the sector's practices and frameworks. However, these practices continue to change as new legislative challenges appear, such as the recent overruling by the Court of Cassation. Political and legal instability persists while the government simultaneously seeks to ensure

IRAQ TRENDS AND DEVELOPMENTS

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better processes for local and foreign investors. By keeping informed about legal and economic developments and adhering to regulatory requirements, investors can adapt their strategies and capitalise on opportunities in Iraq's growing sectors.



Law and Practice

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FIVERS Studio Legale e Tributario is an Italian independent law firm founded in 2014. It assists financial and real estate-sector clients and listed issuers with corporate M&A and the management of litigation. Its corporate clients include some of the leading Italian and international companies. The firm's strategy consists of enhancing the specific skills of its professionals in the different areas of legal and tax prac-

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Authors



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1. Introductory

1.1 Forms of Corporate/Business Organisations

The Italian legal system encompasses a variety of corporate/business forms, each with differing levels of liability, governance and capital requirements.

A preliminary distinction may be drawn between:

- partnerships (*società di persone*), where participants are often also directors and have unlimited liability;
- capital companies (*società di capitali*), where directors may also be non-participants and participants have limited liability (save for extraordinary circumstances provided for under applicable law); and “hybrid” companies, which have two categories of participants: participants with unlimited liability and management powers (*accomandanti*) and participants without management powers and limited liability.

Partnerships are mostly used for small-sized enterprises and may be set up as:

- *società in nome collettivo* (SNC), a general partnership where all partners have unlimited liability); or

- *società semplice* (SS), the simplest form of partnership used primarily for professional or agricultural activities. An SS is not allowed to engage in commercial business activities and its partners have unlimited liability.

Capital companies may be set up as:

- *società a responsabilità limitata* (SRL), a limited liability company mostly used for small to medium-sized enterprises (SMEs), where corporate capital is divided into quotas (not shares), the participants are referred to as “quota-holders” and corporate governance rules are flexible; or
- *società per azioni* (SPA), a joint stock company mostly used by medium to large-sized enterprises and those wishing to access capital markets, where corporate capital is divided into shares and corporate governance rules are more rigid and must follow one of three possible governance models (see **3.1 Bodies or Functions Involved in Governance and Management**). “Hybrid” companies may be set up as:
 - *società in accomandita semplice* (SAS), where corporate capital is divided into quotas (and not shares); or
 - *società in accomandita per azioni* (SAPA), where corporate capital is divided into shares.

The categories above are indicative, as Italian corporate law allows further customisation of the corporate governance rules within a company's by-laws, and capital companies may also be used for small-sized enterprises with a direct involvement of participants in the management (typical of partnerships).

Further distinctions may be drawn within some of the different corporate forms indicated above, depending – for instance – on the corporate purpose (eg, if the company pursues a lucrative or mutualistic purpose), business activity (eg, an SPA may be used as collective investment undertaking in the form of a SICAF (ie, investment company with fixed capital) or a SICAV (ie, investment company with variable capital), access to capital markets (ie, non-listed and listed companies).

It is also possible to set up a company in Italy in the form of *societas europea* or European Company, pursuant to Council Regulation No 2157/2001.

For the sake of clarity, in this chapter the focus will be on the rules applicable to SPAs and ordinary SRLs (ie, not considering the special rules applicable to so called “*simplified SRL*”, the “*SME SRL*” and the “*Innovative Start-up SRL*”), as these are the most common forms of corporate organisations.

The analysis will also be limited to rules applicable to the generality of Italian companies, without regard to special sector laws.

The corporate governance rules applicable to Italian companies listed on an Italian regulated market (hereinafter simply referred to as “*listed companies*”) will be considered, not including a comprehensive analysis of the rules applicable

to companies listed on Italian multilateral trading facilities (MTF), which are set forth under the applicable listing rules.

1.2 Sources of Corporate Governance Requirements

The principal source of corporate governance requirements for Italian companies is the Italian civil code (the “*Civil Code*”).

The general corporate governance structure of each company is reflected in its deed of incorporation and by-laws. Each company may adopt further internal rules and policies on specific aspects of its corporate governance (eg, board internal regulation, shareholder meeting regulation).

An Italian listed company is also subject to specific corporate governance laws, and most notably:

- Part IV of the Unified Financial Code (“*UFC*”, Legislative Decree 58/1998), an overarching legislative decree regulating the financial sector;
- second-level regulations issued by the Italian market authority, Consob (most notably, Consob Regulation No 11971/1999 on issuers; Consob Regulation No 17221/2010 on related parties’ transactions; and Articles 15 to 18 of Consob Regulation No 20249/2017, setting forth requirements for listed entities in specific situations);
- guidelines, Q&As and notices issued by Consob; and
- further EU and Italian laws and regulations regarding specific aspects that may impact corporate governance, such as market abuse regulation (Regulation EU 596/2014 and relevant delegated and implementing EU and

Italian regulations) and financial audit (Legislative Decree No 39/2010).

The Italian Stock Exchange (*Borsa Italiana S.p.A.*) has also set forth specific corporate governance rules applying to any company whose securities are listed on its markets.

Italian listed companies may also voluntarily decide to adopt corporate governance codes sponsored by regulated markets and/or private associations. As of the end of 2023, 97% of Italian companies on the regulated market managed by the Italian stock exchange, (representing 99% of market capitalisation of those companies) adopted the “*Corporate Governance Code*” of the Italian Corporate Governance Committee, which brings together issuers’ associations (ABI, ANIA, Assonime, Confindustria), the Italian Stock Exchange and professional investors’ association (*Assogestioni*) (the “*Code of Corporate Governance*”).

Pursuant to Italian Law (ie, Legislative Decree 231/2001), a legal entity may be liable for specific crimes committed in their interest or to their benefit by individuals in senior positions or under their direction or supervision. To avoid liability, an entity may adopt and effectively implement an “*Organisational Model*”, designed to identify and prevent the risks of commission of a long list of potential criminal offences on behalf of or in the interest of the company, establish protocols for decision-making and internal controls and appoint a supervisory body (*Organismo di Vigilanza*) tasked with monitoring the Model’s effectiveness and compliance.

Companies operating in specific regulated sectors are also subject to EU and Italian corporate governance laws and regulation, including banks (eg, Bank of Italy Circular No 285/2013),

insurance companies (eg, Legislative Decree No 209/2005), financial intermediaries and asset management companies.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Below is a summary of specific corporate governance requirements applicable to listed SPAs, divided between mandatory and voluntary requirements.

Mandatory Requirements

Italian listed companies are subject to stricter and mandatory corporate governance requirements under Italian law, including on:

- appointment of members of the board of directors and of the board of statutory auditors through a slate-voting mechanism, aimed at ensuring that the minority shareholders have a right to appoint at least one candidate (Articles 147-ter and 148 of the UFC);
- appointment of a minimum number of independent directors in the board of directors;
- rules to ensure gender diversity in the board of directors and the board of statutory auditors (ie, at least two-fifths of their members must be of the “*less-represented gender*”)
- stricter integrity requirements for directors;
- appointment of a financial reporting officer responsible for fair accounting and financial disclosures (Article 154-bis of UFC);
- the adoption of a policy on related parties’ transactions (Consob Regulation No 17221/2010);
- the adoption of internal rules and procedure to comply with market abuse regulations (eg, rules on insider list and internal dealing, management of inside information) and disclosure obligations of inside information;

- lower quorums for shareholder meetings and thresholds for the exercise of shareholders' rights (eg, right to call a meeting and submit voting proposals) and to initiate derivative suits and challenge shareholders' resolutions;
- specific rules on proxy voting and participation through "*designated representative*";
- binding shareholders' vote on the remuneration policy of the company and non-binding shareholders' vote on directors' remuneration (so called "*say-on-pay*")
- wider disclosure obligations with respect shareholder meetings (eg, obligation to include a report on the items on the agenda) and longer notice period;
- additional reporting obligations, including semi-annual financial reporting (see **6.1 Financial Reporting**), annual "*report on corporate governance and ownership structure*" and "*remuneration report*";
- increased transparency on shareholder ownership and shareholders' agreements.

Even Italian companies listed on an Italian MTF are subject to stricter and mandatory corporate governance requirements under Italian law than those applicable to non-listed companies. For instance, an Italian SPA that intends to be listed on the Euronext Growth Milan market (an MTF managed by the Italian Stock Exchange) must comply with specific corporate governance rules set forth in the relevant listing rules, including for instance:

- appointment of at least one independent director;
- the adoption of a policy on related parties' transactions;
- mandatory shareholders' vote for major business transactions; and

- disclosure obligations (in addition to those applicable pursuant to mandatory EU and Italian laws on market abuse).

In addition to the requirements above, companies operating in specific regulated sectors (eg, banks, financial intermediaries and asset management companies) are also subject to additional corporate governance requirements under EU and Italian laws (eg, appointment of board committees).

Voluntary Requirements

As indicated above, the large majority of Italian listed companies have adopted the Code of Corporate Governance.

Adoption of the rules of the Code is voluntary; an issuer that has formally adopted the Code of Corporate Governance may decide not to comply with specific rules of the Code, if it provides an explanation thereof (so-called "*comply or explain*" principle).

Each listed company must indicate in an annual "*report on corporate governance and ownership structure*" whether it has adopted a corporate governance code and highlight and explain any decision to depart from any of its provisions.

The Code of Corporate Governance includes several principles and recommendations, including for instance on:

- the role of the board to pursue "*sustainable success*" and promote dialogue with shareholders and other stakeholders;
- the adoption of a procedure for the internal and external management of documents and information concerning the company (including inside information);
- the board's composition and diversity;

- the appointment of independent directors and annual assessment of their independence;
- the adoption of internal rules and procedures that define the functioning of the board and its committees;
- the appointment of “*lead independent director*” in specific instances, who has the task of collecting and co-ordinating the requests and contributions of non-executive directors and co-ordinating the meetings of the independent directors;
- the appointment of board committees with informative, propositional and consultative functions, and in particular:
 - (a) a Control and Risk Committee;
 - (b) a Remuneration Committee; and
 - (c) a Nomination Committee;
- conducting of a periodic self-assessment by the board;
- guidelines for remuneration policies for executive directors and top management; and
- the adoption of an internal control and risk management system.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In the last months there has been an intense debate among legal scholars and operators on the following “*hot topics*” regarding the corporate governance of listed companies:

- the fiduciary duties of the board of directors of a target company in the context of a hostile takeover and their legal obligation of “*passivity*” (ie, refrain from potentially defensive activity without the consent of the shareholder agreement, as provided by Article 9 of EU Takeover Directive, Directive 2004/25/EC);
- the significant limitations and procedural hurdles imposed by a recent legal reform on an

- incumbent board of directors for the presentation of a slate of candidates for the appointment of a new board of directors; and
- the ambiguities of the Italian law that entitles the Italian government to exercise a veto right and/or impose restrictions on the acquisition of Italian companies operating in strategic sectors (so called “*golden power*”), and the significant leeway that such golden power allows the government.

2.2 ESG Considerations

With the Legislative Decree No 125/2024, the Italian legislature has implemented the EU Corporate Sustainability Reporting Directive, or CSRD (Directive EU 2022/2464), which requires large companies and listed SMEs (excluding so-called micro-enterprises) and parent companies of large groups to prepare and publish an annual comprehensive report on sustainability, in accordance with the European sustainability reporting standards (ESRS), covering environmental and social impacts, governance frameworks, sustainability-related risks and opportunities, and strategic objectives.

The new legislation has introduced the role of the sustainability auditor, who is required to provide assurance on a company’s sustainability reporting, ensuring its accuracy and compliance with regulatory requirements and standards like the ESRS.

The schedule for the entry into force of the new reporting obligations is different, depending on the different category of each relevant entity.

Other than the new rules implementing the CSRD, there is not a general reporting obligation on ESG matters.

However, companies may decide to voluntarily adopt ESG principles and provide periodic information on the implementation of such principles. Some companies may also decide to voluntarily adopt international standards such as the Global Reporting Initiative (GRI), Sustainability Accounting Standards Board (SASB) or the Task Force on Climate-related Financial Disclosures (TCFD) to enhance transparency and credibility in their ESG communication.

A company may also decide to include in its corporate purposes the pursuit of the interest of other stakeholders (ie, other than the shareholders), including those of the employees, clients, suppliers, creditors, public administration and society in general. Pursuant to a specific set of rules adopted by the Italian legislature (Law No 208/2015, paragraph 1, Sections 376 to 384), these companies may therefore adopt the status of so-called *società benefit*, be included in a special registry and become subject to specific annual reporting (so-called impact reporting), to be annexed to the annual financial statements.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management SPA

As indicated above, the corporate governance of an SPA may be based upon three possible models.

So-called traditional model

The “*traditional model*” is the most common and default governance model. It is comprised of a management body (a sole director or a board of directors) and a control collective body (ie, the board of statutory auditors), both appointed by the shareholder meeting.

Typically, the board of directors has a general management and strategic role and delegates specific managerial powers to a chief executive officer and/or to one or more additional executive directors and/or an executive committee. The board of statutory auditors has a control function and is required to ensure that the company’s management is in compliance with the law, the by-laws and with the principles of proper management, and in particular with respect to the adequacy of the organisational, administrative and accounting structure of the company. Furthermore, the board of statutory auditors may be required to conduct the financial audit of the company, if the company has not appointed an external auditor or audit firm (see **7.1 Appointment of External Auditors**).

The two-tier model

The two-tier model is inspired by the German governance system, and contemplates a supervisory board appointed by the shareholder meeting and a management board, appointed by the supervisory board.

An external auditor or audit firm mandatorily conducts the statutory financial audit.

A one-tier model

The one-tier model contemplates a single management body appointed by the shareholder meeting, which includes in itself an internal audit committee participated in by independent directors.

An external auditor or audit firm mandatorily conducts the statutory financial audit.

In companies subject to a mandatory financial audit (eg, listed companies), the supervisory body – board of statutory auditors, supervisory board or internal audit committee, depending

on the governance system – is also required to serve as audit committee pursuant to Legislative Decree 39/2010 (which implemented EC Directive 2006/43) and in that capacity monitor the financial reporting process and effectiveness of internal control, internal audit and risk management systems.

Since most of the Italian SPAs have adopted the traditional model, the authors will limit their analysis to the corporate governance rules applicable to the traditional model.

See **4.1 Board Structure** for a more detailed description of the structure of a board of directors in an SPA with the “*traditional*” governance model.

A company (typically, a large-sized SPA and less frequently an SRL) may appoint a general manager (*direttore generale*), a top manager with wide managerial powers and responsibilities. The general manager may be appointed in alternative or in addition to the CEO.

SRL

In an SRL, the by-laws contemplate a wide range of possible management structures:

- sole director;
- a board of directors; and
- multiple directors, with joint or separate powers.

An SRL is not required to appoint a supervisory body (ie, sole auditor or board of statutory auditors) or an external auditor, unless it exceeds certain dimensional thresholds set out in Article 2477 of the Civil Code, is required to prepare consolidated financial statements, controls a company subject to mandatory statutory audit,

or it is required to do so by special laws (eg, due to its specific business activity).

In an SRL, corporate governance rules are more flexible and depend heavily on the by-laws.

3.2 Decisions Made by Particular Bodies

Typically, the board of directors defines the overall strategy (eg, the business plan) and organisational structure of the company. The board appoints the chairperson (if the chairperson is not appointed by the shareholders), the board committees, and defines the overall strategy and organisation of the company.

The board may delegate managerial powers to a chief executive officer, one or more executive directors, or an executive committee, provided that under Italian law some matters may not be delegated by the board of directors, such as (Article 2381, paragraph 4, Civil Code):

- issuance of convertible bonds;
- approval of the draft annual financial statements;
- approval of capital increases;
- resolutions regarding capital losses; and
- merger and demerger proposals.

Board committees perform informative, propositional and consultative functions vis-à-vis the board.

3.3 Decision-Making Processes

SPA

In an SPA with a board of directors, the decision-making process typically follows these steps:

- the chairperson calls the board meeting pursuant to the by-laws. Generally, by-laws provide that a board meeting must be con-

vened, if so requested by a minimum number of directors;

- the board members meet in person and/or through distance connection (as provided under the by-laws). Unless provided otherwise in the by-laws, the meeting is validly held if the majority of directors in office are present and resolutions are taken by a majority vote of those present; and
- resolutions are recorded in the minutes of the meeting, which are signed by the chairman and the secretary and included in an official book of board resolutions.

In an SPA, board resolutions may not be taken through circular resolutions (unlike in SRL).

SRL

In an SRL with a board of directors, board resolutions may be taken through board meetings in person or through distance connection (likewise in an SPA) as well as by circular resolutions (ie, “*written consultation*” or “*express written consent*”). However, resolutions regarding specific matters are taken only through a board meeting (the approval of draft financial statements, merger and demerger projects and a capital increase).

All resolutions must be recorded in an official book.

4. Directors and Officers

4.1 Board Structure

In an SRL and an SPA the chairperson is appointed by the shareholders/quota-holders or by the board itself.

Once appointed, the board of directors may then appoint among its members:

- a chairperson (if the chairperson was not appointed by the shareholders);
- a chief executive officer and one or more executive directors, granting them delegated powers;
- an executive committee, granting it delegated powers; and
- board committees (eg, remuneration committee, risk and control committee, nomination committee).

The appointment of internal committees is required pursuant to EU and Italian laws for companies operating in specific sectors (eg, banks and management companies), or recommended by codes of corporate governance (eg, Corporate Governance Code).

Typically, in a board of directors there are executive directors, that have specific roles in the company or are entrusted with delegated powers, and non-executive directors.

In listed companies as well as those operating in related sectors (eg, banks, financial institutions and management companies) the board must also include a minimum number of non-executive and independent directors.

As indicated above **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**, the Corporate Governance Code also recommends the appointment of a lead independent director in specific instances, who has the task of collecting and co-ordinating the requests and contributions of non-executive directors and co-ordinating the meetings of the independent directors.

4.2 Roles of Board Members

In an SPA, all directors are required to perform their duties with diligence and in an informed

manner. They must request any necessary information from the CEO and executive directors and propose any required action if they become aware and/or have grounded suspicion of any possible prejudicial facts or anomalies. Directors are also required to comply with “*principles of proper management*”, following general criteria of economic rationality over time identified by business science and assessing the adequacy of a company’s organisation, as well as its administrative and accounting structure based on the information received.

Independent directors (where appointed) are expected to play a key role within the board of directors, exercising a check-and-balance function as well as contributing to the overall discussions with their perspective.

The CEO and the executive directors are required to fulfil their duties and exercise their delegated powers with diligence. They also have a duty to inform the entire board of directors and the board of statutory auditors, at least at the intervals set forth in the by-laws and in any event at least once every six months, on the general performance and outlook, as well as on the most significant transactions of the company and its subsidiaries, in terms of size or characteristics. They are also required to ensure that the organisational, administrative and accounting structure is appropriate to the nature and size of the company.

The chairperson is responsible for calling and setting the agenda of the meetings of the board of directors, co-ordinating the meetings and ensuring that all directors are provided with adequate information on the items on the agenda. These tasks are further developed by the Corporate Governance Code. Companies operating in specific business areas (eg, banks and financial

institutions) are also subject to specific requirements pursuant to sector laws (eg, in a bank the chairperson cannot have executive roles).

The board of directors may also appoint board committees, with investigative, propositional and consultative functions regarding specific areas. The area of competence of each committee is indicated in the by-laws and/or in internal regulations approved by the board of directors. The appointment of board committees is recommended for listed companies pursuant to the Code of Corporate Governance and required under specific sector laws (eg, banks and financial institutions).

The general principles set forth above apply also to an SRL.

4.3 Board Composition Requirements/Recommendations

Italian corporate law does not mandate any composition requirements or recommendations for an SRL and a non-listed SPA (except for those subject to sector laws, such as banks and financial institutions).

Listed companies are subject to specific composition requirements under Italian law, as indicated in **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**, including on the appointment of directors by minority shareholders, appointment of independent directors and gender diversity.

The Code of Corporate Governance also recommends (Article 2) that in a listed company:

- the board should be comprised of executive and non-executive directors;
- the directors should have professional skills and competence that are appropriate to their

tasks and the number and skills of non-executive directors should ensure significant influence in the decision-making process of the board and guarantee an effective monitoring of management;

- a significant number of non-executive directors should be independent (in general, at least two independent directors; in larger companies with a concentrated ownership structure, at least one-third of the board; in other larger companies, at least half of the board);
- the company should apply diversity criteria to the composition of the board of directors, ensuring the primary objective of adequate competence and professionalism of its members; and
- each company should define the diversity criteria for the composition of the board of directors and the control body, and identify the most suitable tool for their implementation, considering its ownership structures.

It bears noting that listed companies are required to include in their annual “*report on corporate governance and ownership structure*” description of the diversity policies applied in relation to the composition of the administrative and control bodies or explain the reasons why they decided not to adopt any diversity policy (unless the information is referred to in the “*sustainability report*”, see **2.2 ESG Considerations**).

Specific composition requirements are also mandated pursuant to specific sector laws (eg, banks and financial institutions).

4.4 Appointment and Removal of Directors/Officers

In SPA and SRL, a person that has been disqualified or declared bankrupt or sentenced to a penalty involving a prohibition to hold public

office or managerial roles may not be appointed director (Article 2382 of the Civil Code). Additional requirements apply to listed SPAs (as set forth in Ministerial Decree 162/2000) as well as to companies subject to specific sector laws (eg, directors of banks are required to comply with so-called fit and proper requirements).

Under Italian law, the mechanisms for appointing and removing directors vary depending on the corporate form and whether a company is listed, as indicated below.

SRL

In an SRL, directors are appointed and may be removed through a vote of the quota-holders, unless the by-laws provide otherwise (Article 2475 of the Civil Code).

SPA

Directors are appointed by the ordinary shareholder meeting (Article 2383 of the Civil Code). The by-laws may entitle specific categories of shareholders and/or holders of participation financial instruments with a right to appoint directors. Directors may be removed any time by the shareholder meeting, provided that in the event of a removal without cause the removed director is entitled to damages.

In a listed SPA, the appointment of directors by the shareholder meeting is conducted through a slate-voting mechanism provided in the by-laws (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**), designed to ensure representation of minority shareholders (Article 147-ter UFC). The composition of the board of directors must comply with specific gender diversity requirements.

4.5 Rules/Requirements Concerning Independence of Directors

Italian corporate law does not require companies to appoint independent directors, except for listed companies and entities subject to sector laws (eg, banks, financial institutions), as indicated above (1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares). It bears highlighting that an SPA is required to appoint a board of statutory auditors, which has a control function and whose members must be independent.

There are rules and requirements under general Italian corporate law designed to regulate situations of potential conflicts of interests, as indicated below.

SPA

Italian corporate law prohibits directors of an SPA from engaging in activities that compete with the company. In particular, directors may not act as unlimited liability partners in competing firms, undertake competing activities on their own or on behalf of others, or serve as directors or general managers of competing companies, unless expressly authorised by the shareholder meeting (Article 2390 of the Civil Code). This authorisation may be general, prior, or implicit in the appointment resolution. A breach of this prohibition exposes a director to dismissal and liability for damages.

Directors and members of supervisory boards of companies operating in the credit, financial and insurance sectors are also subject to an “*interlocking ban*” (Article 36 of Law Decree 201/2011), that limits their right to hold management, supervisory or top executive roles in competing firms.

Italian corporate law also requires directors to disclose any personal interest, whether direct or on behalf of third parties, in transactions undertaken by the company to the other directors and statutory auditors (Article 2391 of the Civil Code). This obligation applies even if the relevant interest is not in conflict with the company (eg, if the company and the director have a concurring interest in a transaction).

An “*interested*” director must disclose the nature, terms, origin and extent of the interest. Once a personal interest is disclosed, the relevant director is not required to abstain from voting on the matter. Instead, the board is required to justify the transaction thoroughly, explaining its benefits. A duty to abstain exists for directors of an SPA operating in specific sectors (eg, banks and financial institutions), if they hold an interest that conflicts with the interest of the company.

If the CEO holds a personal interest, they must abstain from executing the transaction.

If the company is managed by a sole director, they must disclose their interest to the shareholder meeting.

The board is collectively liable if a resolution lacks proper reasoning or fails to consider potential consequences and the “*interested*” director may be individually liable for any damage resulting from failure to disclose its interest.

Directors may also be liable if they misappropriate corporate opportunities or confidential information learned through their role (Article 2391, paragraph 5, Civil Code).

SRL

The rules under Italian corporate law on conflict of interests of directors in an SRL are less strict

than those applicable in an SPA (Article 2475-ter Civil Code).

In particular, in the event a director has a personal interest in conflict with the company, a resolution of the board of directors may be challenged by the other directors and auditor(s) if:

- the vote of the relevant director in conflict was decisive for the quorum; and
- the resolution causes financial damage to the company.

Moreover, any contracts executed on behalf of the company by a director with an interest in conflict with the company (whether it is a personal interest or an interest on behalf of another third party) may be annulled at the request of the company if the conflict was known or recognisable by the counterparty.

4.6 Legal Duties of Directors/Officers

The main legal duties of directors of an SPA pursuant to the Italian Civil Code may be summarised as follows.

- Duty of care – directors must fulfil their duties pursuant to applicable laws and by-laws with care, consistently with the nature of their office and their individual skills (Article 2392, paragraph 1, of the Civil Code).
- Duty to act in an informed manner – directors must base their decisions on adequate information and request that any necessary information be provided to the board of directors (Article 2381, paragraph 6, of the Civil Code).
- Duty to intervene – directors who become aware of potentially prejudicial facts must act to prevent or mitigate damages (Article 2392, paragraph 2, of the Civil Code).

- Duty of loyalty – directors must perform their duties with independence of judgement, directing their action to the pursuit of the company purpose
- Duty of proper management – directors must ensure adherence to general business rationality and contribute to the implementation of an adequate organisational, administrative and accounting structure.

In addition to the general duties applicable to all directors, delegated executive directors are also subject to the following additional general duties.

- Duty to ensure organisational adequacy – delegated executive directors must ensure that a company's organisation and administrative and accounting structures are adequate considering its nature and size (Article 2381, paragraph 5, of the Civil Code).
- Duty to inform – delegated executive directors must periodically report to the board of directors and the board of statutory auditors on company performance and its foreseeable prospects, as well as on significant transactions carried out by the company and its subsidiaries (Article 2381, paragraph 5, of the Civil Code).

The same general duties indicated above may be applied to the directors of an SRL (Articles 2475 and 2476 of the Civil Code).

4.7 Responsibility/Accountability of Directors

Directors owe their duties primarily to the company, its shareholders (or quota-holders, in an SRL) as well as to its creditors (as to the capacity of the company to pay its debts).

The by-laws of a company may also require directors to pursue the interest of other stakeholders, including employees, clients, suppliers, creditors, public administration and society in general (ie, so-called *società benefit*).

It bears noting that according to the Code of Corporate Governance, a listed SPA should pursue “*sustainable success*”, aiming at creating long-term value for the benefit of the shareholders, “*taking into account the interests of other stakeholders relevant to the company*”.

4.8 Consequences and Enforcement of Breach of Directors’ Duties

Under Italian law, the rules regarding the enforcement of directors’ duties and claims for damages differ depending on the corporate form.

SPA

The directors are liable for damages against the company, its shareholders (or quota-holders, in an SRL) and creditors in the event of a breach of their duties.

In an SPA, the following claims for damages may be brought against directors in the event of a breach of their duties:

- claim for damages on behalf of the company, pursuant to:
 - (a) a resolution by the shareholder meeting; or
 - (b) a resolution by the board of statutory auditors;
- claim for damages on behalf of the company, initiated by minority shareholders (at least 20% of the capital or the percentage set forth in the by-laws in a non-listed SPA; at least 2.5% of the capital or the lower percentage set forth in the by-laws, in a listed company);

- claim for damages by the company’s creditors (if the ability of the company to pay its debts has been infringed); and
- claim for damages by individual shareholders and/or third parties (in the event they have been directly affected by a breach of the directors’ duties).

In case of insolvency, the legal actions under the first three bullet points above may be initiated by the officer responsible for the relevant insolvency proceeding.

SRL

In an SRL, the following legal actions may be brought against directors in the event of a breach of their duties:

- claim for damages by any quota-holder (regardless of their participation);
- claim for damages by the company’s creditors (if the ability of the company to pay its debts has been infringed); and
- claim for damages by individual quota-holders and/or third parties (in the event they have been directly affected by a breach of the directors’ duties).

According to prevailing case law and majority of legal scholars, a claim for damages may also be brought against the directors on behalf of the company as well as, in case of insolvency, by the officer responsible for the relevant insolvency proceeding.

Parent Companies

Where a company – either an SPA or SRL – controls and exercises direction and co-ordination over another company and there is a breach of the “*principles of proper corporate and business management*”, the directors of the parent com-

pany may be liable jointly with the parent company itself vis-à-vis:

- the participants in the controlled entity, for any damages to the profitability and value of the participation; and
- the creditors of the controlled entity, as to the capacity of the company to pay its debts).

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In addition to the cases indicated under 4.8 Consequences and Enforcement of Breach of Directors' Duties, in case of a breach of corporate governance requirements a director may also be subject to:

- administrative fines, for breaches of specific corporate governance-related administrative obligations (eg, omissions in the registration of corporate resolutions in the Companies' Registry); and
- criminal liability, for specific corporate-governance related criminal offences (eg, false communications to the public, fraudulent influence on the shareholder meeting).

Criminal and administrative liability is generally non-waivable.

On the other hand, civil liability for damages of a director vis-à-vis the company and shareholders may be mitigated through an insurance policy (so-called "*Directors and Officers*" Insurance Policy). The shareholders may also decide to grant a waiver to the directors for any potential liability (eg, through a vote of the shareholder meeting), in relation to events and circumstances that occurred beforehand (whereas a pre-emptive discharge of liability is not admissible).

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

In an SPA, the shareholder meeting resolves upon the remuneration of the directors and no specific restrictions apply. If so provided under the by-laws, the shareholder meeting may resolve upon the aggregate remuneration of all directors and leave it to the board to split the total amount among the board's members. The remuneration of directors with specific offices indicated in the by-laws is decided upon by the board of directors, in consultation with the board of statutory auditors.

In a SRL, it is up to the by-laws to set forth the rules regarding the remuneration of directors (absent any specific provisions on this matter in the Civil Code).

In a listed SPA, the shareholder meeting is also required to:

- approve a remuneration policy for directors, general manager, key officers and members of the board of statutory auditors; and
- any remuneration plan based on financial instruments (eg, a stock option plan) for directors and employees of the company, its parent company, or controlled companies.

Specific restrictions on remuneration of directors and employees are provided pursuant to special sector laws (eg, banks, financial institutions), including with respect to the ratio between variable and fixed components as well as cash or instrument-based forms of remuneration.

4.11 Disclosure of Payments to Directors/Officers

In an SRL and in a non-listed SPA the remuneration of directors and officers is disclosed within

the annual financial statements, on an aggregate basis.

Each listed SPA must issue “*remuneration report*”, providing a comprehensive description of any remuneration paid to each director and member of the board of statutory auditors, and in aggregate for other key personnel. This “*remuneration policy*” is put to a non-binding vote of the shareholder meeting (ie, the so called “*say on pay*”).

Specific disclosure requirements on directors’ remuneration apply to companies operating in regulated businesses pursuant to sector laws (eg, banks).

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The relationship between the company and its shareholders is of contractual nature and is regulated in the relevant incorporation deed and by-laws as well as in mandatory provisions of Italian corporate law.

Each SPA is required to keep and regularly update a record of the shareholders of a company, which is not publicly available and may be consulted by the shareholders. In addition, each non-listed SPA is required to file with the Company’s Registry a list of its shareholders on an annual basis (within 30 days from the approval of the financial statements), which is publicly available.

In an SRL, there is a record of the quota-holders, which is registered with the Companies’ Registry and publicly available.

5.2 Role of Shareholders in Company Management

In general, shareholders of an SPA are excluded from the management of the company (unless a shareholder is also appointed director or officer of the company). However, the by-laws may provide that specific management decisions require an authorisation of the shareholders.

In an SRL, quota-holders may be directly involved in the management of the company, as provided in the by-laws (eg, the by-laws may provide that the directors must be quota-holders and/or that specific management decisions are resolved upon by the quota-holders).

5.3 Shareholder Meetings

The Italian civil code reserves certain decisions to the shareholder meeting (eg, the appointment of the board of directors, the board of statutory auditors and external auditors; changes to the by-laws; merger, demerger and liquidation proceedings). In both an SPA and an SRL, a shareholder meeting is to be held at least on an annual basis for the approval of the annual financial statements and when the term of office of the board of directors and board of statutory auditors has expired.

The rules that govern the holding and conduct of shareholder meetings differ depending on the corporate form and whether the company is listed or not listed.

SPA

In an SPA, a shareholder meeting may be “*ordinary*” or “*extraordinary*”, depending on the relevant subject matters. “*Ordinary*” meetings require lower quorums and are not in notarial form, whereas “*extraordinary*” meetings require higher quorums and must be in notarial form.

Typically, the board of directors or the chairman (the board of statutory auditors, in case of inaction) call the meeting with a notice that indicates the place and time of the meeting and the agenda.

In a non-listed SPA, the notice may be sent by email or any other means to each shareholder at least eight days in advance or, alternatively, be published in an official publication (the Official Gazette) or at least one newspaper at least 15 days in advance.

A listed SPA is required to publish the notice at least 30 days in advance and post it on the company's website (or a different period, as required for specific items on the agenda), together with a report explaining the items on the agenda.

If so provided under the by-laws, the meeting may take place anywhere in Italy or even abroad, as well as by means of telecommunication.

At the opening of the meeting, the chairperson is required to identify the attendees, their entitlement to participate (in person or by proxy), the reaching of the relevant quorum and the validity of the meeting.

The chairperson appoints a secretary, who is tasked with the drafting of the minutes of the meeting.

The chairperson conducts the meeting, leaves the floor to the managers that are called to explain the different items and/or shareholders that intend to intervene, puts the items on the vote and proclaims the result of each vote.

In a listed SPA, the by-laws may entitle the board of directors to provide that the shareholders may participate in a meeting only through a design-

nated proxy (ie, the shareholders may vote only through voting instructions given to the designated proxy ahead of the meeting).

The minutes of each meeting are signed by the chairperson and the secretary and included in the official book of shareholder meetings.

SRL

The rules governing the holding and conduct of quota-holder meetings in an SRL are very flexible. The by-laws of each SRL may determine the means and timing for the calling of a meeting.

5.4 Shareholder Claims

Shareholders are entitled to claim damages against the directors, in the event of a breach of their duties, as well as against the parent company (if it exercises direction and co-ordination over the company) and its directors, in case of breach of the *"principles of proper corporate and business management"* (see 4.8 **Consequences and Enforcement of Breach of Directors' Duties**).

5.5 Disclosure by Shareholders in Publicly Traded Companies

In general, under Italian law, each person is required to notify the Market Authority (Consob) and the relevant listed company whenever it acquires or reduces its participation above or under specific thresholds of the voting share-capital (ie, 3%, 5%, 10%, 15%, 20%, 25%, 30%, 50%, 66.6% and 90%). For SMEs (small and mid-size enterprises), the initial threshold is reduced to 5%.

Disclosure obligations also apply when a person acquires a significant *"long position"* on the shares of a listed company through financial instruments, derivatives and other contracts (subject to specific thresholds and exemptions).

The disclosure includes the identity of the first person/entity at the beginning of the ownership chain. See **6.3 Companies Registry Filings** as to the disclosure of the beneficial owners of a company pursuant to applicable anti-money laundering regulation.

In addition to the disclosure obligations above, any person acquiring a participation above the 10%, 20% and 25% thresholds in the voting share capital of a listed company are also required to disclose additional information, including its future plans regarding the company for the subsequent six months and the origin of the funds used for the acquisition.

The shareholders of an Italian listed company are also required to disclose the existence and content of any shareholders' agreement (including any subsequent changes and termination).

Specific disclosure requirements apply to shareholders that have launched a takeover bid or that have triggered the thresholds of the mandatory takeover bid.

Specific disclosure requirements apply also to institutional investors and asset managers as to their engagement, investment strategies and management agreements, in furtherance of specific provisions of Italian law implementing the EU "*Shareholders' Right Directive II*" (those provisions also impose specific disclosure requirements on proxy advisers).

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting Non-Listed SPAs

A non-listed SPA is required to prepare and publish financial statements on an annual basis. A non-listed SPA is not required to approve any interim financial reporting, unless so required by the company's by-laws and/or sector laws.

Draft annual financial statements are drawn up by the management body of the SPA (eg, the board of directors) and approved by the shareholder meeting within 120 days (or 180 days under specific conditions) after the end of each financial year (Articles 2423 and subs. of the Civil Code).

Listed SPAs

A listed SPA is subject to enhanced transparency and periodic reporting requirements under Italian law (primarily, the UFC).

In particular, a listed SPA is required to publish:

- annual financial statements, which are drawn up by the management body of the SPA (eg, the board of directors) and approved by the shareholder meeting within 120 days (or 180 days under specific conditions) after the end of each financial year (Articles 154-ter of UFC and 2423 and subs. of the Civil Code); and
- half-yearly financial statements, which are drafted and approved by the management body (not approved by the shareholders) within three months from the end of the first semester of the financial year.

A listed SPA may also decide to voluntarily publish further periodic financial statements, if dis-

closure requirements set forth in Consob's Issuer Regulation are complied with (Article 82-ter).

Publication of interim financial statements may be required by the Italian Stock Exchange for specific market segments (eg, companies listed on the Euronext STAR Milan segment of the Italian Stock Exchange are required to publish quarterly financial statements).

In specific circumstances (eg, companies in financial distress), Consob may mandate a listed company to publish additional periodic financial statements, on a monthly or quarterly basis (Article 114, paragraph 5, UFC).

Even an SPA that is listed on an MTF (and not listed on an Italian regulated market) may be subject to enhanced transparency and periodic reporting requirements, as required by applicable listing standards. For instance, an Italian SPA listed on the Euronext Growth Milan market (an MTF managed by the Italian Stock Exchange) is required to publish not only annual financial statements (like any other SPA), but also half-yearly financial statements.

Parent Companies

Under Italian law (ie, Articles 25 and subs. of Legislative Decree No 127/1991, which implements EU Directive 83/349/EEC), an SPA or SRL that controls another entity is required to publish consolidated financial statements on an annual basis, unless specific exemptions apply.

SRLs

An SRL is required to prepare and publish financial statements on an annual basis and is not required to approve any interim financial reporting (unless so required by the company's by-laws and/or sector laws).

Draft annual financial statements are drawn up by the management body of the SRL and approved by the quota-holders within 120 days (or 180 days under specific conditions) after the end of each financial year (Article 2478-bis of the Civil Code).

6.2 Disclosure of Corporate Governance Arrangements

Non-listed companies are not required to disclose their corporate governance arrangements in any periodic report. However, the deed of incorporation and the by-laws of any SRL and SPA are registered with the Companies' Registry and publicly available.

Listed companies are required to issue every year a comprehensive "*report on corporate governance and ownership structure*", including detailed information on their shareholding and corporate governance arrangements, including (among others) information on the main features of the risk management and internal control systems in place in relation to the financial reporting process, the functioning of the shareholder meeting, composition and functioning of the administrative and control bodies and their committees, and a description of the diversity policies applied (Article 123-bis of the UFC).

This report should also indicate whether a company adheres to a corporate governance code (explaining also the reasons for any decision to depart from any provision of a code to which it has adhered) as well as the actual corporate governance practices adopted by it.

Listed companies are required to disclose and post on their website any shareholders' agreement that has been notified to it by the relevant shareholders.

6.3 Companies Registry Filings

SPA and SRL are incorporated and registered with the competent Companies' Registry, which is managed by the local Chamber of Commerce.

The incorporation of an SPA and an SRL requires a notarial deed in front of a notary (even through a videoconference with respect to an SRL and subject to specific restrictions) and the filing of the relevant incorporation deed and of the by-laws attached thereto with the Companies' Registry.

Italian companies are required to file a long list of documents and information with the Companies Registry, which are then publicly available. These documents and information include (without limitation):

- deed of incorporation, by-laws and any amendments thereof;
- appointment, cessation, revocation, of directors and members of the board of statutory auditors;
- transfer of the corporate seat;
- grant or revocation of powers of attorney;
- minutes of shareholder meetings approving extraordinary transactions and approving the annual financial statements;
- annual financial statements and consolidated financial statements;
- the fact that the company has (or ceased to have) a sole participant;
- the fact that the company is subject to the direction and co-ordination of another entity (Article 2497-bis Civil Code);
- documentation regarding extraordinary transactions (eg, merger, demerger, transformation);
- liquidation and appointment of liquidators;
- in a listed SPA, any shareholders' agreement; and

- in an SRL only, any transfers of quotas and any update to the quota-holders' list.

Italian Anti-Money Laundering Law requires companies to disclose the identity of their beneficial owner to the Companies' Registry. However, this obligation is currently suspended pursuant to a court order and a case is pending in front of the Court of Justice of the European Union.

Failure to make required filings may have different consequences, depending on the nature of the actual filing:

- some corporate acts must be filed to produce any legal effect and are void until the relevant filing is completed and processed (eg, incorporation deed and amendments of the by-laws); and
- some other corporate acts are unenforceable against third parties until the relevant filing is completed and processed.

A failure to complete a required filing within the relevant deadline may also lead to pecuniary fines against directors, statutory auditors and the general manager (Article 2630 of the Civil Code).

Company directors may be held personally liable for damages suffered by the company, shareholders or third parties due to their failure to file required documents (eg, pursuant to Articles 2395, 2476 and 2497-bis of the Civil Code).

The Companies' Registry exercises a formal and administrative review of the documentation and information provided to it, without any substantive legal review. The Companies' Registry may reject the registration of a corporate act, if it lacks formal mandatory requirements or appears

to be unauthentic or filed by a person void of relevant powers.

A more substantive legal review is carried out by the notary with respect to deeds in notarial form (eg, deed of incorporation, amendments to the by-laws, minutes of shareholders' extraordinary resolutions).

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

An external auditor is an official auditor or audit firm, included in a special registry held by the Ministry of Economy and Finance, appointed by a company to conduct the financial audit of the financial statement of a company. This external auditor is separate from the board of statutory auditors, which is a control body required in each SPA with the so-called traditional governance model.

In an SPA with the so-called traditional governance model, the board of statutory auditors is required to conduct the audit of the financial statements, unless an external auditor is appointed.

An SPA appoints an external auditor voluntarily or when required to do so pursuant to applicable law (eg, the company (i) has issued instruments listed on a regulated market; (ii) is required to prepare consolidated financial statements, (iii) is a regulated entity, (iv) is controlled by, controlling or jointly controlled by, an entity indicated under previous letters (i)-(iii)).

The relationship between the company and the external auditor is governed by a set of statutory, contractual and professional rules, which contemplates for instance:

- the appointment by the shareholder meeting based on a proposal of the board of statutory auditors;
- the maximum length of each appointment, different for non-listed and listed companies and companies operating in specific sectors);
- cases in which the appointment of an external auditor may be revoked for cause;
- duties of diligence and care; and
- relations with the board of statutory auditors.

Considering the limitations applicable to an SRL's ability to access the trading venues and to conduct regulated business, most often an SRL appoints an external auditor if it is controlled by or controls a company that is required to appoint an external auditor.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

As indicated in 4.6 **Legal Duties of Directors/Officers**, each director is required to *"evaluate, on the basis of the information received, the adequacy of the organisational, administrative and accounting structure of the company"* (Article 2381, paragraph 3, of the Civil Code), ensuring adherence to general business rationality, as well as to contribute to the implementation of an adequate organisational, administrative and accounting structure.

Consistently with this general duty, each director is required to ensure that the company has in place a system of risk management and internal controls, that are adequate and reasonably proportioned to the specific business activity and dimensions of the company.

This obligation is more stringent in a listed SPA, for which the Code of Corporate Governance recommends that the board of directors should

(among others) define the overall system of internal controls and risk management and supervise its adequacy, assign responsibilities to a control and risk committee, and appoint a Head of Internal Audit, who reports functionally to the board.

Specific obligations in connection with the management of risk and internal controls apply to companies subject to special sector laws (eg, banks, financial institutions).

Contributed by:

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Henlin Gibson Henlin provides advice and assists clients with corporate compliance matters. The firm also advises on board and committee composition, including board diversity, leadership structures, as well as board functions and duties, codes of ethics and other governance-

related materials designed to comply with legal and regulatory requirements and best practices. The firm specialises in commercial matters, including corporate and shareholder litigation issues.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The principal forms of business organisations in Jamaica are:

- sole traders or sole proprietors;
- partnerships – general or limited, joint ventures;
- private companies limited by shares;
- public companies limited by shares;
- companies limited by guarantee with or without a share capital;
- companies having unlimited liability; and
- branches of overseas corporations.

1.2 Sources of Corporate Governance Requirements

The principal source of corporate governance requirements for companies in Jamaica are:

- the Companies Act, 2004 (as amended);
- the PSOJ Corporate Governance Code, 2021;
- the PSOJ Navigating Corporate Governance A Comprehensive Handbook and Toolkit, 2024;
- the Jamaica Stock Exchange Rules;
- the Jamaica Stock Exchange Corporate Governance Index Manual, 2020;
- the Corporate Governance Framework for Public Bodies;
- the OECD Guidelines on Corporate Governance; and
- the Trust and Corporate Services Providers Act, 2017.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

The corporate governance requirements that exist for companies with shares that are pub-

licly traded are based on the principles in the Jamaica Stock Exchange Rules and Rulebooks, Corporate Governance Index Framework and the PSOJ Corporate Governance Code which takes into account whether the company has regulations or policies that cover the following.

- Shareholder rights – the rights of shareholders including access to information, participation in shareholder meetings, approval of board remuneration, shareholder views or management of the control structure of the company.
- Fair and equitable treatment of shareholders – promotes the equitable treatment of shareholders. This takes into account the allocation of voting rights and effective mechanisms for minority shareholder participation including the ability to influence board composition, insider trading or disclosure of related-party transactions and adequate notices of shareholder meetings.
- Stakeholders and corporate governance – stakeholder participation takes account of the attention given to employee welfare, employee membership on boards, whistle-blowing policies, environmental issues and employee share option schemes or opportunities.
- Disclosure and transparency – the form of ownership and structure of the company in a manner that promotes openness, trust and transparency including the form of owner structure as well as the role and importance of the audit function, and the extent to which the policies are disclosed in the annual reports or on company websites.
- The board of directors – the responsibilities of the board including its oversight of policies relating to governance, disclosure and ethics, meeting frequency, the composition of the board as between independent and non-independent directors, the existence of board

committees and the independent evaluation of board performance.

- For publicly listed companies, compliance with Jamaica Stock Exchange (JSE) requirements – the JSE’s regulations including whether they conform to acceptable industry standards such as the IFRS, disclosure of the top ten shareholders, connected parties of directors, shareholders and senior management, communications and timely disclosures, updated website with the company’s mission, vision and financial performance.

All the requirements listed above are desirable and, in the case of the JSE rules, mandatory.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance Corporate Services Providers: Licensing

Corporate Services Providers are required to acquire a licence to provide Corporate Licensing and Operations as a business as at 25 April 2022. The Trust and Corporate Services Providers Act, 2017 sets out that entities must apply to the Financial Services Commission (FSC) within 12 months thereafter (by 24 April 2023) for the grant of their licence if they currently provide the following services:

- act as a co-ordinator or an assistant in the formation, management or administration of a firm or company;
- act as (or arranging for another person to act as) a director or secretary of a company, an alternate director or a partner of a firm;
- provide a registered business office, business address, correspondence address or administrative address for a company, firm or any other person;

- act as (or arranging for another person to act) as a nominee shareholder for another person;
- arrange the establishment of any legal entities not covered by any of the foregoing services and providing any of the foregoing services to such entities; and
- perform any other service that the Minister may, by order published in the Gazette, prescribe as a corporate service.

Other entities that wish to provide corporate services are required to await the grant of their licence before performing these services.

Failure to acquire a licence as a Corporate Service Provider from the FSC is an offence and can lead to prosecutorial and/or monetary liability to the person, corporate body, or the relevant officer of the corporate body.

Beneficial Ownership Requirements

The Companies (Amendment) Act, 2023 was passed on 1 March 2023, to comply with international best practices to combat money laundering and terrorist financing. The amendment is focused on creating a risk-based approach to identifying the beneficial ownership of legal persons and ultimately creating greater transparency in corporate governance.

The new obligations under the Companies (Amendment) Act, 2023 require all companies to:

- identify the beneficial owner by examining the structure of the company. This is now determined through:
 - (a) ultimate ownership – owns 25% or more interest or voting rights;
 - (b) ultimate effective control – the ability to determine company policy, or appoint or remove directors; and
 - (c) highest management authority – high-

ranking management official to include chief executive officer, general manager, chief operations manager or chief financial officer;

- collect and maintain accurate, adequate and up-to-date records on beneficial ownership of the company;
- notify the Registrar of Companies of any changes to the beneficial ownership information;
- keep the beneficial ownership information for a minimum of seven years from the day of the last business transaction; and
- conduct due diligence assessments to verify beneficial ownership information.

There are sanctions for failure to comply with these obligations including monetary penalties or being removed from the Register of Companies. This ultimately affects the company's compliance status and ability to do business.

2.2 ESG Considerations

Reporting on ESG is considered in the context of the role of stakeholders in corporate governance. Operating in a post-pandemic era, there is a host of new social and environmental issues that stakeholders must address. There is growing concern about employee mental health, combating communicable diseases in shared workspaces and adapting to post-lockdown workplace performance. ESG considers whether there are board-approved policies as to how environmental issues are to be addressed or handled. Companies are evaluated on the existence of the policies as well as their availability for inspection such as in the annual reports, on the website or any other publicly accessible source.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies or functions involved in the governance and management of a company are:

- the board of directors;
- board committees;
- the company secretary;
- shareholders in general meetings; and
- senior management and the CEO or managing directors.

Board committees support the board in carrying into effect the policymaking, governance and strategic objectives. There are different types of board committees, such as audit and remuneration, corporate governance, risk management and corporate social responsibility committees.

3.2 Decisions Made by Particular Bodies The Board of Directors

The board of directors is responsible for the company's business, stewardship and strategic direction. Board power is kept in check by shareholders in a general meeting. They make decisions in relation to:

- nomination of board members;
- appointment of board members to fill casual vacancies;
- appointment and removal of the company secretary;
- addressing conflicts of interest;
- auditor-related issues other than their appointment;
- treasury, risk management, capital and internal controls;
- dividend policy and payments;
- communications and disclosure;

- accounting and management control policies and practices including the signing of cheques, promissory notes and other negotiable instruments;
- appointment and termination of directors and senior management;
- acquisition and disposal of major assets;
- budget, strategy, mission and vision; and
- major contracts and investments.

The following resolutions are subject to the approval of the board:

- determining and amending the operational and financial strategic objectives of the company;
- determining and amending key performance indicators in support of the strategic objectives (including, for example, any financial ratios); and
- any other matters that Jamaican laws or regulations or the company's articles of incorporation require the board to approve.

Other Decision-Makers

The board committees support the board within the scope of their terms of reference.

The company secretary does not make decisions. The company secretary is the administrative office of the company. The secretary ensures a company's compliance with its articles, governing legislation and regulations, for example, preparation of returns and filings with the Registrar of Companies, filings with the JSE for public companies and maintenance of the company's registers.

Shareholders are the ultimate decision-makers in companies. They exercise their powers in general meetings. The following powers are reserved to them:

- the appointment, removal and remuneration of auditors;
- the appointment, removal and remuneration of directors; and
- the amendment of articles.

3.3 Decision-Making Processes

In the decision-making process:

- the board of directors makes decisions at meetings by resolutions or consensus – resolutions may also be made as written resolutions, if required by the articles;
- written resolutions are required for important decisions such as borrowing or otherwise committing the company;
- board committees make decisions by consensus and in accordance with their terms of reference;
- the company secretary makes only such decisions as are authorised by the board or terms of appointment;
- shareholders make decisions by resolutions in extraordinary general meetings and annual general meetings by resolutions or consensus – resolutions may also be made as written resolutions, if permitted by the articles; and
- senior management, CEOs and managing directors make decisions to carry into effect the policy and strategic directions of the board and within its authorised limits.

Meetings

All meetings must be convened on proper notice and must be quorate. Directors or shareholders entitled to attend and vote at meetings may waive procedural irregularities in the giving of notice. The quorum requirements cannot be waived.

Extraordinary general meetings or special meetings may be called by the directors at any time

or at the request of the shareholders to conduct any business which needs to be conducted in between annual general meetings.

The directors' and shareholders' meetings are presided over by a chairman.

Questions, Votes and Resolutions

Questions arising at shareholder meetings are determined by a majority of votes except where in relation to the special resolution in Section 138 (2) of the Companies Act, which provides that a majority vote is three fourths of all the members present and entitled to vote in person or by proxy.

In cases of an equality of votes, the chairman may, depending on the chairman, have either a second or casting vote.

Article 64 of Table A of the Companies Act provides that at any general meeting a resolution put to the vote of the meeting must be decided on a show of hands unless a poll is demanded by:

- the chairman;
- at least three members present in person or by proxy;
- any member(s) present in person or by proxy and representing not less than one tenth of the total voting rights of all the members having the right to vote at the meeting; or
- a member(s) holding shares of the company being shares on which an aggregate sum has been paid up equal to not less than one tenth of the total sum paid up on all the shares.

4. Directors and Officers

4.1 Board Structure

The structure of the board of directors is as follows:

- chairman;
- vice chairman;
- independent directors; and
- non-independent directors.

4.2 Roles of Board Members

The chairman presides over board meetings and ensures their orderly conduct, sets the agenda for meetings and leads the discussions, appoints all committee chairs and recommends committee members. The chairman usually maintains strong communication with the chief executive officer and maintains corporate integrity.

The CEO functions as the senior executive officer responsible for ensuring that decisions of the board are implemented and that the organisation functions effectively and efficiently.

Non-executive directors help develop and approve proposals on strategy. They are mostly involved in policymaking decisions and provide independent oversight and constructive challenge to the executive directors.

It is not uncommon for the board of directors to only have a chairman because of the small nature of a company.

4.3 Board Composition Requirements/Recommendations

The requirements and recommendations for boards of directors are as follows. Each board member should:

- be independent of each other;

- be able to assess the company's overall policy and strategy;
- have adequate knowledge of the environment in which the company operates and its associated risks; and
- have subject-matter expertise to enable the performance of their role as a board member.

Regarding the board as a whole:

- the composition of the board should match the intended board composition as to diversity in gender and expertise;
- at minimum, the board should be comprised of members with expertise in governance, general finance, business, accounting, law, human resources, cybersecurity, privacy and management; and
- the board should be transparent as to the number of directors who should be independent.

4.4 Appointment and Removal of Directors/Officers

Appointments may be made by directors to fill casual vacancies and by the shareholders in a general meeting. In either case, they are appointed by ordinary resolution.

There is, subject to the provisions of the Companies Act and the articles of incorporation, a requirement for the staggered retirement of directors except at the first annual general meeting where all the directors must retire. In all subsequent years, one-third of the directors must retire, if there are multiples of three. If there are no multiples of three, the number nearest to one-third shall suffice. Each year, it is the longest-serving directors who shall be required to retire. If two directors were appointed simultaneously, the director to retire is chosen by lot.

Directors may also be removed pursuant to Section 179 of the Companies Act prior to the expiration of their term of office. Directors can also be removed in accordance with the articles, where they:

- cease to be a director by virtue of Section 177 of the Companies Act;
- become bankrupt or make arrangements or compositions with their creditors generally;
- become prohibited from being a director by reason of any order made under Sections 180 and 182 of the Act;
- become of unsound mind;
- resign by notice in writing to the company; or
- have been absent for more than six months without permission of the directors from meetings of the directors held during that period.

Section 177 deals with the duty of directors who are entitled to be directors by virtue of a share qualification. Section 180 sets out the procedure by which directors may be removed by the court. Section 182 sets out the considerations by the court for the disqualification of the directors which includes persistent breaches of the Act.

4.5 Rules/Requirements Concerning Independence of Directors

The Companies (Amendment) Act, 2017, incorporates the common law duty of directors *"to avoid circumstances which, whether directly or indirectly, constitute a conflict of interest or may result in a conflict of interest with the interests of the company"*.

The duty is not infringed by mere interest or relationship. The Act provides that this duty is not infringed if the circumstances cannot reasonably be regarded as likely to give rise to a conflict of interest or if the matter giving rise to the circum-

stances has been approved by the directors. A conflict of interest arises for example if a director is also a director of a competitor company. A director has a duty to disclose the nature of their interest at a meeting of the directors where they are directly or indirectly interested in a matter which may constitute a conflict of interest or may result in a conflict of interest with the interests of the company. The necessary quorum must be met at the meeting without including the director in question.

Additionally, pursuant to Section 193 (1), directors or officers must disclose their interests in a contract or proposed contract. They must disclose the nature and extent of their interest in writing to the company or request to have this information entered in the minutes of the meetings of the directors.

Disclosure

The disclosure by a director must be made at the meeting at which a proposed contract is first considered or at the first meeting after they become interested in a contract or proposed contract. A person who has interests in a contract and thereafter becomes a director must disclose their interest at the first meeting of the directors. The same is true for an officer of the company.

A record of this contract must be kept at the registered office of the company. The contract is subject to the approval of the board of directors of the company, and subject to the provisions of the First Schedule. It is important to note that the director concerned must not be present during any deliberations of the board in connection with that approval.

Voting

Article 90 (2) of Table A of the Companies Act provides that a director must not vote in respect of any contract or arrangement in which they are interested, and if they must do so their vote must not be counted, nor must they be counted in the quorum present at the meeting.

The PSOJ Corporate Governance Code, 2021, recommends that the board identify, in its disclosures, each board member that it considers to be independent. The board should determine whether a director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. It also recommends that the board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including if the director:

- has been an employee of the company or group within the last three years;
- has or has had, within the last three years, a material business relationship with the company, either directly or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;
- has received or receives additional remuneration from the company apart from a director's compensation, and participates in the company's share option or a performance-related pay scheme;
- has close family ties with any of the company's advisers, directors or senior employees;
- holds cross-directorships or has significant links with other directors through involvement in other companies or bodies; or
- represents a significant shareholder.

Former CEOs

A former CEO will not qualify as an independent director unless there has been a period of at least three years between the date on which they ceased employment with the company as CEO and the date of their appointment to the board.

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors and officers of a company are contained in the Companies Act. The Act stipulates that every director and officer of the company in exercising their powers and discharging their duties must:

- act honestly and in good faith with a view to the best interest of the company; and
- exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances, including, but not limited to, the general knowledge, skill and experience of the director or officer.

Directors have a duty to avoid circumstances which directly or indirectly constitute a conflict of interest.

4.7 Responsibility/Accountability of Directors

Directors owe their duties to the company alone.

However, in determining what the best interests of a company are, a director or officer may have regard to the interests of the company's shareholders and employees and the community in which the company operates.

4.8 Consequences and Enforcement of Breach of Directors' Duties

A director may be removed or required to pay damages if there is a breach of duty.

If a director's breach causes harm to the company, the following persons may enforce the action on behalf of the company:

- a member or former member of a company or affiliated company;
- a debenture holder or former debenture holder of a company or an affiliated company; or
- a director or former director or officer of a company or an affiliated company.

These are complainants pursuant to Section 212 (3) of the Companies Act.

A complainant may apply to the court for leave to bring a derivative action in the name of the company and on behalf of the company for the purpose of prosecuting, defending or discontinuing an action on behalf of the company.

The result of this is that the court may make an order as it deems fit, including:

- authorising the complainant, the Registrar or any other person to control the conduct of the action;
- giving directions for the conduct of the action;
- directing that any amount adjudged payable by a defendant in the action be paid, in whole or in part, directly to former and present shareholders or debenture holders of the company or its subsidiary, instead of to the company or its subsidiary; or
- requiring the company or its subsidiary to pay reasonable legal fees incurred by the complainant in connection with the action.

The harm caused to the company will be remediated including restoring any loss sustained by the company.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Section 213A of the Companies Act makes provision for action to be taken against the directors or officers of the company where it is alleged by a complainant that:

- an act or omission of the company or any of its affiliates effected a result;
- the business or affairs of the company or any of its affiliates are or have been carried on or conducted; or
- the powers of the directors of the company or any of its affiliates are or have been exercised in a manner that unfairly disregards, or is unfairly prejudicial or oppressive to, any shareholder or debenture holder, creditor, director or officer of the company.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Shareholder or member approvals are required in connection with the remuneration, fees or benefits payable to directors. Article 82 of Table A of the Companies Act, 2004 provides that the remuneration of the directors must, from time to time, be determined by the company in general meeting. The remuneration is deemed to accrue from day to day. The directors may also be paid all travelling, hotel and other expenses properly incurred by them in attending and returning from meetings of the directors or any committee of the directors or general meetings of the company, or in connection with the business of the company.

The directors have the power to determine the remuneration of the company secretary and the managing director or chief executive officer.

4.11 Disclosure of Payments to Directors/Officers

Guided by the Jamaica Stock Exchange Rules and the PSOJ Corporate Governance Code, public companies are required to state in their annual report the components of director remuneration including whether a director received or receives additional remuneration from the company apart from director's fees, or participates in its share option scheme or any performance-related pay or profit-sharing scheme or guarantees on termination.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Shareholder Rights

Shareholders do not participate in the day-to-day management of the company. They own while the directors manage. However, they exercise ultimate control in general meetings. In the period between meetings, however, they have certain rights. These include:

- the right to access financial records;
- the right to inspect the financial records; and
- the right to inspect a company's books and records.

Section 157 of the Companies Act provides that:

- the auditors must make a report to the members on the accounts examined by them, and on every balance sheet, every profit and loss account and all group accounts laid before the company in general meeting during their tenure of office, and the report must contain statements as to the matters mentioned in the Seventh and Eighth Schedules; and

- the auditors' report must be read before the company in general meeting and must be open to inspection by any member.

Under the Companies Act, shareholders have the right to sue directors and officers of the company for breach of their duties or for acting in a manner that is inimical to or disregards their interests.

Voting Rights and Shareholder Powers

Shareholders have voting rights. This is the method by which they ultimately participate in corporate decision-making, including the right to appoint directors, make proposals and vote for structural changes such as acquisitions or liquidation.

The articles of incorporation reserve certain powers to the shareholders. These powers are exercised in general meetings. Shareholders have the right to attend general meetings of the company where the directors present the company's annual report and comment on its performance over the year. At the annual general meeting and extraordinary general meetings, shareholders may, among other things, elect new directors, discuss directors' remuneration, and ask questions regarding the company's future.

Shareholders can require directors to convene extraordinary general meetings if they are the holders of one-tenth of the paid-up capital of the company.

Shareholders also have the right to transfer ownership. They have the option of quickly liquidating shares into cash by selling their shares. The right to transfer the shares is usually subject to pre-emptive rights. This means that existing shareholders have the right to be offered

the shares prior to selling them to external third parties.

5.2 Role of Shareholders in Company Management

See 5.1 Relationship Between Companies and Shareholders.

5.3 Shareholder Meetings

Shareholder meetings are required. Section 126 of the Companies Act provides that every company must in each year hold a general meeting as its annual general meeting in addition to any other meetings in that year, and must specify the meeting as such in the notices calling it; and not more than 15 months must elapse between the date of one annual general meeting of a company and that of the next.

The first annual general meeting can be held within 18 months of incorporation. If the company does this, it does not have to hold a meeting in the year of incorporation.

The Act stipulates that the directors of a company, notwithstanding anything in its articles, must, on the requisition of members of the company holding not less than one-tenth of the paid-up capital of the company, at the date of the deposit, which carries the right of voting at general meetings of the company – or, in the case of a company not having a share capital, members of the company representing not less than one tenth of the total voting rights of all the members having at that date a right to vote at general meetings of the company – proceed duly to convene an extraordinary general meeting of the company.

The requisition must state the objects of the meeting and must be signed by the requisitionists and deposited at the registered office of the

company. If the directors do not within 21 days from the date of the deposit of the requisition proceed duly to convene a meeting, the requisitionists, or any of them representing more than half of the total voting rights of all of them, may themselves convene a meeting, but any meeting so convened must not be held after the expiry of three months from that date. Also, a meeting convened by the requisitionists must be convened in the same manner, as nearly as possible, as that in which meetings are to be convened by directors. Additionally, in the case of a meeting at which a resolution is to be proposed as a special resolution, notice of the meeting must be given in order for the meeting to be duly convened.

The Statutory Meeting and Statutory Report

Section 127 of the Companies Act prescribes that every company limited by shares and every company limited by guarantee and having a share capital must, between one month to three months from the date at which the company is entitled to commence business, hold a general meeting of the members of the company, which must be called “*the statutory meeting*”. The directors must, at least seven days before the day on which the meeting is held, forward a report (referred to as “*the statutory report*”) to every member of the company.

The statutory report must be certified by not less than two directors of the company or where there are less than two directors, by the sole director, and must state:

- the total number of shares allotted, distinguishing shares allotted as fully or partly paid up other than in cash, and stating in the case of shares partly paid up the extent to which they are so paid up, and in either case, the

consideration for which they have been allotted;

- the total amount of cash received by the company in respect of all the shares allotted;
- an abstract of the receipts of the company and of the payments made, up to a date within seven days of the date of the report, exhibiting under distinctive headings the receipts of the company from shares and debentures and other sources, the payments made, and particulars concerning the balance remaining in hand, and an account or estimate of the preliminary expenses of the company;
- the names, addresses and descriptions of the directors, auditors, if any, managers, if any, and secretary of the company; and
- the particulars of any contract, the modification of which is to be submitted to the meeting for its approval, together with the particulars of the modification or proposed modification.

The directors must deliver to the Registrar a certified copy of the statutory report for registration after sending the report to the members of the company. Also, the directors must make a list showing the names, descriptions and addresses of the members of the company, and the number of shares held by them respectively, to be produced at the commencement of the meeting and to remain open and accessible to any member of the company during the continuance of the meeting. Section 127 (10) states that the section does not apply to private companies.

Voting at Meetings and Giving Notice

The Companies Act describes the notice that must be given for any shareholder meeting. In the case of the annual general meeting, this is 21 days’ notice in writing and in the case of a meeting other than an annual general meeting or a meeting for the passing of a special resolu-

tion, 14 days' notice in writing, in the case of a company other than an unlimited company; and seven days' notice in writing in the case of an unlimited company.

A meeting of a company called by a shorter notice period indicated may be deemed to have been duly called if it is so agreed in the case of a meeting called as the annual general meeting, by all the members entitled to attend and vote at the meeting; and in the case of any other meeting, by a majority in number of the members having a right to attend and vote at the meeting, being a majority together holding not less than 95% in value of the shares giving a right to attend and vote at the meeting, or, in the case of a company not having a share capital, together representing not less than 95% of the total voting rights at that meeting of all the members.

Section 129 of the Companies Act requires 21 days' notice for calling an annual general meeting and 14 days' notice in writing in the case of a meeting other than an annual general meeting or for the passing of a special resolution.

Section 130 requires that notice of the meeting must be served on every member of the company.

The court may make orders for the calling or conduct of meetings where it is impractical to do so in any manner in which meetings of the company may be called.

5.4 Shareholder Claims

See 4.6 Legal Duties of Directors/Officers and 4.9 Other Bases for Claims/Enforcement Against Directors/Officers.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Shareholder disclosures are not required except where those shareholders are directors or senior management. See 6. Corporate Reporting and Other Disclosures.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Section 145 of the Companies Act states that companies are obligated to provide shareholders with an annual report card on the financial position of the company. They must place before the annual general meeting a profit and loss account or an income and expenditure account, a balance sheet with a directors' report attached, and an auditor's report.

In accordance with JSE Rule 407, public companies are required to submit to the JSE two hard copies and one electronic copy of their quarterly financial statements at intervals not exceeding three months and within 45 days of the end of the period to which the statements relate. Directors, senior management, their connected person shareholdings and the shareholdings of those persons holding ten of the largest block of shares must be included in the financial report.

The quarterly financial statements must be approved by the board of directors and signed by two or more directors of the company and should state whether or not they are audited or unaudited. Companies with quarterly filings that are 45 days overdue shall have the trading in their shares suspended until the reports are submitted to the stock exchange.

A company that is unable to comply with the JSE quarterly reporting requirement in a timely manner must notify the JSE where it can be foreseen that there is the probability of a delay, and the circumstances and probable extent of the delay. Simultaneously, the company should place an advertisement in the print media advising shareholders of the delay.

Listed companies have the option of submitting their quarterly results as follows:

- fourth-quarter financials be submitted in 45 days (unaudited) and 90 days (audited); or
- audited financial results submitted in 60 days.

Listed companies are required to indicate to the stock exchange and the market which of the two options would be chosen at the beginning of the third quarter each year. However, if there is no change in the option previously chosen, no communication is required.

6.2 Disclosure of Corporate Governance Arrangements

Rule 414 of the JSE Rules requires listed companies to adopt and disclose corporate governance guidelines.

The PSOJ recommends that the companies listed on the JSE describe, in their annual report and accounts, their corporate governance from two perspectives: the first dealing generally with their adherence to the Corporate Governance Code's main principles, and the second dealing specifically with the explanations for non-compliance with any of the Code's provisions. These descriptions together should provide shareholders with a clear and comprehensive picture of a company's governance arrangements in relation to the Code as a criterion of good practice.

6.3 Companies Registry Filings

Every company must deliver to the Registrar successive annual returns which are made up no later than the anniversary date of the incorporation of the company or the anniversary of the last return that was delivered. Each return must be delivered to the Registrar within 28 days after the date on which it is made up.

Every company having a share capital must also deliver to the Registrar a return containing a list of all persons who are members of the company and of all persons who have ceased to be members since the date of the last return or, in the case of the first return, of the incorporation of the company.

In respect of the beneficial ownership of a company, or an intended company, a beneficial ownership return must be filed:

- when forming a company;
- upon the delivery of a return of allotments, in respect of each allottee named therein;
- by a company and delivered to the Registrar annually within 28 days after the date on which it is made up; and
- within 14 days after any change of beneficial ownership information that occurs before the next annual filing of the return is due.

A beneficial ownership return must include the following information:

- the date on which it is made up;
- the name of the company, address of the registered office and, in the case of an overseas company, its principal place of business;
- an accurate, adequate and up-to-date list of all persons who, on the date of the return, are members and beneficial owners of the company, and of all persons who have ceased to

- be members and beneficial owners since the date of the last return or, in the case of the first return of the incorporation of the company;
- the name, date of birth and nationality, address, occupation, taxpayer registration number or other tax identification number or the number, place of issue and expiry date of the valid passport or driver's licence of the beneficial owner;
- in the case of a past member or beneficial owner, the last valid passport or driver's licence held prior to the cessation of membership or ownership of the company, as the case may be;
- in respect of each member who is not an individual, the member's name, date of establishment, nationality, address and taxpayer registration number, or other tax identification number; and
- in the case of a company having shares, the number of shares held by each of the existing members and beneficial owners at the date of the return, specifying the shares transferred since the date of the last return or, in the case of the first return, of the incorporation of the company by persons who have ceased to be members or beneficial owners, respectively, and the dates of registration of transfers.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The company must appoint an external auditor. The Act stipulates that none of the following persons can qualify for appointment as auditor of a company. These are:

- an officer or servant of the company;

- a person who is a partner of or in the employment of an officer or servant of the company; or
- a body corporate.

Section 154 (1) of the Companies Act, 2004, provides that at each annual general meeting, a company must appoint an auditor to hold office from the conclusion of that meeting until the conclusion of the next annual general meeting. The first auditor of a company may be appointed by the directors at any time before the first annual general meeting. An auditor so appointed holds office until the conclusion of that meeting. It is to be noted that the company in general meeting may appoint an auditor if the directors fail to do so.

The auditor of a company has a right to receive notice of every meeting of the shareholders and to attend and be heard at the meeting on matters relating to their duties as auditor. The auditor must make a report to the members on the accounts examined by them, and on every balance sheet, every profit and loss account and all group accounts laid before the company in general meeting during their tenure of office.

The auditor of a company must always have a right of access to the books and accounts and vouchers of the company and is entitled to request any information and explanation from the officers of the company as is necessary for the performance of his duties.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Guided by the Jamaica Stock Exchange Rules and principles in the PSQJ Corporate Governance Code, the board of directors must ensure the implementation of robust risk management

and internal control systems. This includes disclosure in the annual report in a separate segment – Management Discussion and Analysis (MD&A). The MD&A should cover:

- liquidity and capital resources;
- effect of any transactions involving related parties;
- results of operations;
- risk management; and
- present and future prospects of the company.

The MD&A should entail in detail the method by which they have assessed the prospects of the company, over what period they have done so and why they consider that period appropriate. The directors should declare whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of assessment. Also, the board of directors must monitor the company's risk management and internal control system and carry out a review of their effectiveness annually.

Contributed by:

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Nagashima Ohno & Tsunematsu has an established reputation as a leading Japanese law firm in the area of corporate governance. With a team of approximately 75 partners, having various backgrounds ranging from corporate/M&A and capital markets to litigation and investigations, the firm regularly advises on corporate governance matters. It provides practical and strategic advice related to corporate governance based on relevant laws, regulations and guidelines as well as current practices. The key areas of the firm's practice in the corporate

governance sector include conduct of shareholder meetings; proxy statements, securities reports and other disclosure materials; investor relationships; dealing with shareholder activists; management composition and governance structure; management compensation; internal control systems; risk and crisis management; and fiduciary duties, the business judgment rule and directors' liability. The firm primarily advises listed companies in the corporate governance context, but from time to time advises institutional investors as well.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The following are the principal forms of corporate/business organisations in Japan. Explanations found in **1.2 Sources of Corporate Governance Requirements** and later sections focus on the joint stock company unless otherwise indicated.

Joint Stock Company (Kabushiki Kaisha or KK)

A joint stock company is the most commonly used form of corporate/business organisation in Japan. All Japanese listed companies are joint stock companies. This form is commonly used for closely held companies as well. All shareholders of a joint stock company enjoy limited liability up to their respective contribution amounts. This form is not a pass-through entity for Japanese tax purposes.

Limited Liability Company (Godo Kaisha or GK)

The form of a limited liability company is used only for closely held companies. The governance structure and rights of equity holders (including the allocation of profit distributions among equity holders) can be determined in a flexible manner by the articles of organisation, so this form is suitable for joint ventures and wholly owned subsidiaries. All equity holders of a limited liability company enjoy limited liability up to their respective contribution amounts. This form is not a pass-through entity for Japanese tax purposes.

General Partnership Company (Gomei Kaisha) and Limited Partnership Company (Goshi Kaisha)

The form of a general partnership company and that of a limited partnership company are used only for closely held companies, but are not commonly used. General partners in these companies have unlimited liability; limited partners enjoy limited liability. These forms are not pass-through entities for Japanese tax purposes.

Limited Liability Partnership (LLP)

The form of a limited liability partnership is used for joint ventures. The number of limited liability partnerships has been increasing but, despite its pass-through nature for Japanese tax purposes, has not become very popular because of some practical inconveniences arising from its lack of legal personality.

1.2 Sources of Corporate Governance Requirements

There are various sources of corporate governance requirements for companies in Japan. The following are the principal sources.

Companies Act (Act No 86 of 2005, as Amended)

The Companies Act, together with its subordinate regulations, provides the basic corporate governance requirements for companies, whether listed or not. The latest major amendment was made in December 2019.

Financial Instruments and Exchange Act (Act No 25 of 1948, as Amended) (FIEA)

The FIEA, together with its subordinate regulations, requires listed companies and certain other publicly held companies to make disclosures related to corporate governance in various filings.

Securities Listing Regulations Published by the Tokyo Stock Exchange (TSE Regulations)

The TSE Regulations include certain corporate governance requirements which companies listed on the Tokyo stock exchange must comply with. The Tokyo stock exchange has three segments (Prime, Standard and Growth). Companies listed at the Prime Market must meet enhanced corporate governance requirements. Companies listed at the Prime Market, the Standard Market and the Growth Market respectively account for approximately 43%, 41% and 16% among approximately 3,800 companies listed at the Tokyo stock exchange as of April 2025.

Corporate Governance Code

The Corporate Governance Code is a part of the TSE Regulations. The Tokyo stock exchange requires listed companies to “*comply or explain*” with respect to the principles included in the Corporate Governance Code and to disclose some corporate governance matters in their corporate governance reports. The latest amendment to the Corporate Governance Code took effect in June 2021.

Stewardship Code

The Stewardship Code published by the Council of Experts on the Stewardship Code, established by the Financial Services Agency, is another source of important corporate governance requirements, although it is not directly applicable to listed companies but to institutional investors. The Stewardship Code of 2020 is the most recent version. Many major institutional investors have published their own proxy voting policies in response to the Stewardship Code, will vote at shareholder meetings in accordance with their own policies, and will have engagement discussions with the management of listed companies to encourage mid- to long-term growth.

Guidelines and Study Reports

Japanese governmental agencies or study groups organised by them from time to time publish various guidelines or study group reports with respect to corporate governance issues, which include the Corporate Governance System Guidelines, the Fair M&A Guidelines, the Outside Directors’ Guidelines and the Guidelines for Corporate Takeovers.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Listed companies are subject to various corporate governance requirements, including the following.

Governance Structures

Having a board of directors is mandatory. Listed companies must choose one of the three governance structures:

- company with a board of statutory auditors;
- company with an audit and supervisory committee; or
- company with nominating and other committees.

Companies with a board of statutory auditors, companies with an audit and supervisory committee, and companies with nominating and other committees respectively account for approximately 55%, 43% and 2% among approximately 3,800 companies listed at the Tokyo stock exchange as of April 2025.

Outside/Independent Members

All the listed companies are required to have outside director(s) under the Companies Act.

The Corporate Governance Code provides that one third or more of the directors should be inde-

pendent outside directors in the Prime Market (or two or more directors must be independent outside directors in the other markets). If a listed company has a controlling shareholder, enhanced requirements regarding independent outside directors will apply in order to protect the interest of minority shareholders.

Shareholder Proposal Right

Shareholders who hold 1% or more of the total voting rights or 300 or more of the votes for six months or longer may make a proposal of up to ten agenda (including appointment and dismissal of directors) by notifying the company at least eight weeks (or a shorter period if so provided in the articles of incorporation) prior to a shareholder meeting.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In December 2023, the Financial Services Agency amended the subordinate regulations under the FIEA to enhance disclosure requirements related to:

- agreements between a listed company and its shareholder regarding the governance (eg, director nomination right);
- agreements between a listed company and its major shareholder regarding disposal or additional acquisition of shares (eg, standstill); and
- financial covenants included in loan agreements or bond indentures.

Most of these amendments became applicable from April 2025.

In February 2024, the Tokyo stock exchange issued a notification which requires companies

listed at its Prime Market to make public disclosures in English (in addition to Japanese), effective from April 2025.

Recent significant increase of shareholder activism and hostile takeovers in Japan reveals that some updates and reforms are necessary in the regulations regarding the takeover bids and the bulk shareholding reports in the FIEA. In May 2024, the Diet passed the amendment to the FIEA to reform the rules for takeover bids and the bulk shareholding reports. These amendments are expected to become applicable in 2026. Draft amendment to the Stewardship Code is being reviewed taking into account this amendment to the FIEA.

The Legislative Council of the Ministry of Justice started to discuss amendment to the Companies Act, which is to cover some corporate governance issues, including:

- introduction of virtual/online shareholder meetings;
- introduction of the system for confirming the identity of beneficial owners; and
- amendment to the rules applicable to companies with nominating and other committees.

2.2 ESG Considerations

The Corporate Governance Code suggests that a listed company:

- take appropriate measures to address sustainability issues, including social and environmental matters;
- develop a basic policy for the company's sustainability initiatives from the perspective of increasing corporate value over the mid- to long-term; and
- appropriately disclose its initiatives regarding sustainability in its management strategies

and provide information on investments in human capital and intellectual properties.

In particular, a listed company on the Prime Market is encouraged to collect the necessary data to analyse the impact of the risks and earning opportunities related to climate change on its business activities and profits and to enhance the disclosure based on the Task Force on Climate-related Financial Disclosures (TCFD) recommendation or an equivalent framework.

Under the FIEA, publicly traded companies (in this context, listed companies and other companies that are required to file annual securities reports under the FIEA) are required to disclose their notion and efforts on sustainability in annual securities reports. This disclosure requirement spans the following four categories:

- governance;
- strategy;
- risk management; and
- indexes and goals.

In addition, in response to the establishment of the inaugural global sustainability disclosure standards (IFRS S1 and IFRS S2) by the International Sustainability Standards Board in June 2023, the Sustainability Standards Board of Japan established the sustainability disclosure standards (the “SSBJ Standards”) in March 2025. The SSBJ Standards, which can be applied voluntarily at this point, are expected to be adopted in the legal disclosure regime.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management Shareholder Meeting/Directors/Board of Directors

All joint stock companies are required to have a shareholder meeting and directors. If a company has a board of directors, it must appoint three or more directors. A listed company is required to have a board of directors. A company may have one of the following bodies:

- a statutory auditor and, as the case may be, a board of statutory auditors;
- an audit and supervisory committee; and
- nominating and other committees.

If a company has any of a board of statutory auditors, an audit and supervisory committee or nominating and other committees, it must also have a board of directors. A listed company that is a large-sized company (*daigaisha*), ie, a company that has recorded on its audited and approved balance sheet for its most recent fiscal year either JPY500 million or more in stated capital, or JPY20 billion or more in liabilities, is required to have one of these bodies.

Statutory Auditors

The main role of a statutory auditor is to audit the execution of the duties of the directors. A listed company with statutory auditors is required to have a board of statutory auditors.

Audit and Supervisory Committee

An audit and supervisory committee consists of three or more audit and supervisory members, who are also directors of the company elected as such by its shareholder meeting. A majority of the audit and supervisory members must be outside directors. The main role of the audit and

supervisory committee is to audit and supervise the execution of the duties of the directors.

Nominating and Other Committees

Nominating and other committees means a set of a nominating committee, an audit committee and a compensation committee. Each committee consists of three or more directors, and a majority of each committee's members must be outside directors. The main roles of a nominating committee, an audit committee and a compensation committee are, respectively, to determine the candidates for directors, to audit and supervise the execution of the duties of the management, and to determine the compensation of each management member.

In a company with nominating and other committees, an executive officer is supposed to have the broader authority to decide the execution of the company's operation as compared to other types of companies. A representative executive officer appointed from among the executive officers by a board of directors represents the company.

Accounting Auditor

In addition, a large-sized company must have an accounting auditor who is expected to audit the accuracy of the company's financial statements. An accounting auditor must be appointed from among external accounting firms or licensed accountants. A company with an audit and supervisory committee or nominating and other committees is also required to have an accounting auditor.

3.2 Decisions Made by Particular Bodies

The roles of a shareholder meeting and directors may differ depending on whether or not a company has a board of directors. In the case of a company without a board of directors, a

shareholder meeting may adopt any action on behalf of the company, and a director has the broad authority to decide and execute the company's operation.

If a company has a board of directors, the authority of a shareholder meeting is more limited. In this case, the shareholder meeting may adopt only such matters as provided under the Companies Act or the articles of incorporation. A board of directors typically delegates to the representative director and other executive directors the authority to decide the execution of the company's operation except for the matters specifically prescribed under the Companies Act.

Monitoring Model Approach

However, in the case of a company with nominating and other committees, a board of directors may delegate to the executive officer the broader authority to decide the execution of the company's operation, and the matters that the board of directors is required to decide are fairly limited as compared to other types of companies. In this sense, the corporate governance of a company with nominating and other committees is designed as a monitoring model. Likewise, a company with an audit and supervisory committee may take a similar approach if:

- a majority of its directors consist of outside directors; or
- it is so provided in the articles of incorporation.

3.3 Decision-Making Processes

At the board level, unless otherwise provided in the articles of incorporation, a decision by a board of directors is made by a majority of the directors present at a board meeting, as long as a majority of the directors who are entitled to participate in the vote are present. Directors who

have a special interest in the resolution may not participate in the vote. A board meeting may be held through a video-conference or conference call system.

If so provided in the articles of incorporation, a board resolution may be made without holding a physical meeting if all directors who are entitled to participate in the vote agree in writing (whether physically or electronically) to a proposal submitted by a director. That being said, circulation of board minutes to the board members together with their signatures on the minutes is not deemed to be a board resolution.

4. Directors and Officers

4.1 Board Structure

A board of directors consists of three or more directors and is required to appoint one or more representative directors. In the case of a joint stock company with an audit and supervisory committee or nominating and other committees, a majority of each committee's members must be outside directors.

In the case of a company with nominating and other committees, members of each committee may serve as members of other committees.

4.2 Roles of Board Members

The board members are, in general, divided into the following categories:

- representative directors;
- other executive directors; and
- outside directors.

Representative Directors

The role of the representative director is to execute the company's operation and represent the

company. The authority of the representative director extends to all actions (whether judicial or non-judicial) in connection with the company's operation. The representative director may also decide the company's operation to the extent permitted by law as long as the board of directors authorises them to do so.

Other Executive Directors

Other executive directors may not represent the company without a delegation from the representative director but may decide and execute the company's operation, as is the case with a representative director subject to the same condition. However, in the case of a company with nominating and other committees, directors (other than executive officers) are not generally allowed to decide and execute the company's operation because such functions are carried out by an executive officer.

Outside Directors

Outside directors are expected to supervise the management of the company from an independent point of view.

4.3 Board Composition Requirements/Recommendations

A company with an audit and supervisory committee or nominating and other committees must have two or more outside directors. There are several requirements or recommendations for listed companies.

- First, a listed company with a board of statutory auditors is obligated to have one or more outside directors under the Companies Act.
- Second, the Corporate Governance Code recommends that:
 - (a) listed companies on the Prime Market ensure that one third or more of their

directors are independent outside directors; and

- (b) other listed companies appoint at least two independent outside directors.
- Third, the TSE Regulations require listed companies to make efforts to secure at least one independent outside director as a board member.

In addition, the Corporate Governance Code recommends that a board of directors of a listed company be composed in a manner to achieve diversity, including in terms of gender, international experience, work experience and age.

4.4 Appointment and Removal of Directors/Officers

Appointing Directors

Directors are appointed by a resolution of a shareholder meeting. Unless otherwise provided in the articles of incorporation, this resolution must be made by a majority of the votes of the shareholders present at the meeting if a quorum is satisfied (ie, by the presence of shareholders representing a majority of those who are entitled to exercise their voting rights). The company may lower the quorum for the appointment of directors down to a third pursuant to the articles of incorporation.

A cumulative voting system is also available although this is not common in Japan. In the case of a company with an audit and supervisory committee, directors who are audit and supervisory members must be appointed separately from the other directors of the company. Other management members, including an executive officer in a company with nominating and other committees, are appointed by the board of directors.

In addition, the Corporate Governance Code recommends that a listed company, unless it has nominating and other committees or its independent outside directors constitute a majority of its board of directors, seek the involvement of, and advice from, an independent nominating committee regarding the appointment of its directors or other management members. In particular, a listed company on the Prime Market is encouraged to ensure that a majority of such nominating committee's members are independent outside directors and disclose, among other things, the view on the independence regarding the composition of the nominating committee and its authority and roles.

Qualifications of Directors

Although the Companies Act provides the restrictions on qualification of directors that a corporation cannot be a director or an individual who was sentenced for breaching laws and regulations may not become a director during a certain period, there are no nationality or residence restrictions.

Dismissing Directors and Other Members of Management

Directors may be dismissed at any time by a majority of the vote at a shareholder meeting, except audit and supervisory members, whose dismissal requires two thirds of the votes at a shareholder meeting. However, a dismissed director is entitled to seek damages arising out of the dismissal except in cases where justifiable grounds exist. Typically, a dismissed director may claim the compensation they would have received during their remaining term.

In addition, if a director engages in any misconduct or commits a material violation of law or the articles of incorporation in connection with the execution of their duties as a director, and a

proposal to dismiss the director is rejected at the shareholder meeting, then a shareholder holding, for the preceding six months or longer, not less than 3% of the voting rights of all shareholders may file a lawsuit to dismiss the director.

Other management members, including an executive officer in a company with nominating and other committees, may be dismissed by a board of directors. A dismissed executive officer may seek damages, as in the case of a dismissed director.

Statutory Auditors

Statutory auditors are appointed by a majority of the votes at a shareholder meeting. However, dismissal of statutory auditors requires two thirds of the votes at a shareholder meeting. As in the case of directors, a dismissed statutory auditor is entitled to seek damages arising out of the dismissal, except in cases where justifiable grounds exist.

4.5 Rules/Requirements Concerning Independence of Directors

An outside director is a director who does not, in principle, execute the company's operations, and has no relationship with its affiliate companies or their management, etc. A more detailed definition of an outside director is provided in the Companies Act.

Furthermore, the TSA Regulations and the Corporate Governance Code have certain requirements or recommendations in relation to "*independent*" outside directors. An independent outside director is an outside director who satisfies the "*independent officer*" criteria as established by the Tokyo stock exchange. According to these criteria, an outside director who is an executive director or officer of one of the company's main business partners, or an expert

who receives a substantial amount of fees or compensation from the company, is not qualified to be an "*independent*" outside director. In this sense, the "*independent officer*" criteria are more stringent than the "*outside director*" criteria under the Companies Act. Under the Corporate Governance Code, if a listed company on the Prime Market does not appoint such a number of independent outside directors as to constitute one third or more of its directors (or if a listed company on other markets does not appoint two or more independent outside directors), it must publicly explain the reason why. Under the Corporate Governance Code, it is also recommended that a person who has experience managing other companies be included among such independent outside directors.

The Corporate Governance Code also suggests that a listed company with a controlling shareholder appoint such number of independent outside directors who are independent of the controlling shareholder as to constitute at least one third of its directors (in respect of a company listed on the Prime Market, a majority) unless the listed company establishes a special committee composed of independent persons, including independent outside directors, to deliberate and review material transactions or matters that involve a conflict of interest between the controlling shareholder and the minority shareholders.

4.6 Legal Duties of Directors/Officers

Directors owe a fiduciary duty to the company. The Companies Act specifically provides that directors of a company must perform their duties to the company in a loyal manner, with this duty of loyalty being construed as part of a fiduciary duty. As part of their fiduciary duty, directors are required to establish an internal control system of the company. Furthermore, directors have a

duty to supervise other directors' execution of the company's operation.

In connection with the decision on a company's operation, the business judgement rule applies, whereby directors are given broad discretion in making business decisions and are not to be held liable for those decisions unless the business decision or the process thereof is construed as significantly unreasonable.

If a director intends to carry out any transaction:

- with the company;
- that competes with the business of the company; or
- that results in a conflict of interest between the director and the company,

then the director is required to disclose the material facts relating to the transaction to the board of directors and obtain its approval.

4.7 Responsibility/Accountability of Directors

In general, directors owe their duties to the company. However, if a director breaches its fiduciary duty or any other duties, it may be held liable not only to the company but also to any third party that has suffered damage arising from the breach.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Injunctive Relief

If a director engages, or is likely to engage, in an act in violation of law or the articles of incorporation (such acts include breach of a fiduciary duty) and this act is likely to cause substantial damage to the company, a shareholder holding shares in the company for six consecutive months or longer (or a shorter period if so provided in the

articles of incorporation) may seek injunctive relief. In the case of a closely held company, the restriction on the shareholding period does not apply. In the case of a company with statutory auditors, an audit and supervisory committee or nominating and other committees, injunctive relief is granted only if the company is likely to suffer irreparable damage because statutory auditors or the relevant committee members are expected to audit and supervise the directors.

Compensation for Breaches/Third-Party Claims

If a director or a statutory auditor breaches their duties, the company may seek compensation for the damage caused by the breach. In addition, a shareholder may also file a shareholder derivative action on behalf of the company if the shareholder requests that the company file a lawsuit against a breaching director or statutory auditor but the company does not do so within 60 days of such a request. Moreover, if a third party suffers damage arising from the performance of the duties by a director or a statutory auditor who had knowledge that their conduct was inappropriate or was grossly negligent, then the third party may seek recovery of the damage from the director or statutory auditor.

Even if a director or a statutory auditor fails to perform their duties, their liability to a company arising from such failure may be discharged or limited through:

- the consent of all shareholders;
- a resolution of a shareholder meeting; or
- a resolution of a board of directors (or, in the case of a company without a board of directors, consent of a majority of two or more directors) pursuant to the articles of incorporation.

In addition, a director who is neither a representative director nor an executive director or a statutory auditor may enter into an agreement with a company to limit their liability, if so permitted by the articles of incorporation.

Indemnification Agreement/D&O Insurance

A director may enter into a corporate indemnification agreement with a company, pursuant to which in certain circumstances the company indemnifies the director for the costs (including attorneys' fees) and damage that the director has incurred in connection with the performance of their duties. D&O insurance is widely available in Japan. The Companies Act makes clear that in order to enter into a corporate indemnification agreement or D&O insurance, a company needs to obtain an approval of its board of directors or, in case of a company without a board of directors, a shareholder meeting.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In relation to corporate governance, a third party is able to make claims against directors, statutory auditors and other officers for damage incurred in connection with misrepresentations in a company's financial statements, business reports or any other documents unless the directors, statutory auditors or other officers can prove that they have exercised due care. Directors, statutory auditors and other officers of a listed company are also liable for misrepresentations in the public disclosure documents of the company, such as annual securities reports, under the FIEA.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Compensation to Directors

Compensation to directors must be approved by a shareholder meeting unless it is provided in the articles of incorporation. In usual circumstances, a shareholder meeting approves the maximum aggregate amount of compensation of all directors and delegates to the board of directors the authority to decide the compensation to be paid to each director within the approved maximum aggregate amount. In such a case, the board of directors of a listed company with a board of statutory auditors that is a large-sized company or a company with an audit and supervisory committee must approve the policy as to how to determine the specific amount of compensation of each director and disclose this policy in the annual business report. The authority to decide the compensation of each director based upon this policy is often delegated to a representative director or an independent compensation committee.

If the total amount of the compensation of all directors exceeds the maximum aggregate amount of compensation approved by a shareholder meeting, the compensation in excess of the maximum aggregate amount is invalid. In such case, it is considered that the amount of the compensation of each director would be reduced based on a ratio of the total amount of the compensation of all directors to the maximum aggregate amount approved by a shareholder meeting; and a company has a right to request each director to return the excessive amount regardless of its negligence. In addition, the directors involved in such illegal payment are jointly and severally liable to the company for the amount in excess of the maximum aggregate amount approved by a shareholder meeting.

If a company issues its stock or stock options to its directors as compensation, it also needs to obtain the approval of a shareholder meeting on the maximum number of such stock or stock options to be issued and other prescribed details.

In the case of a company with an audit and supervisory committee, the compensation of audit and supervisory members must be determined separately from other directors, and the allocation of compensation among audit and supervisory members is determined based upon their discussion unless a shareholder meeting resolves otherwise or the articles of incorporation provide differently.

In the case of a company with nominating and other committees, a compensation committee determines the compensation of each director and executive officer.

Principles Under the Corporate Governance Code

The Corporate Governance Code recommends that a listed company, unless it has nominating and other committees or its independent outside directors constitute a majority of its board of directors, seek involvement of and advice from an independent compensation committee regarding the compensation of its directors. In particular, a listed company on the Prime Market is encouraged to ensure that a majority of such compensation committee's members consists of independent outside directors and disclose, among other things, the view on the independence regarding the composition of the compensation committee and its authority and roles.

The Corporate Governance Code also considers that listed companies should reflect mid- to long-term business results and potential risks in

determining the compensation of the management and recommends that the proportion of management compensation linked to mid- to long-term results and the balance of cash and stock paid as compensation, respectively, be set appropriately.

Compensation to Statutory Auditors

Compensation to statutory auditors must also be approved by a shareholder meeting unless it is provided in the articles of incorporation. If a company has two or more statutory auditors, compensation of each statutory auditor may be determined based on their discussions, within the maximum aggregate amount of compensation approved by a shareholder meeting or provided by the articles of incorporation.

4.11 Disclosure of Payments to Directors/Officers

A listed company must disclose the compensation of its directors, statutory auditors and other officers in its business report. Such disclosure is required with respect to the total amount of the compensation on a position-by-position basis along with the number of persons appointed to each position, if and to the extent that the amount of the compensation of each individual is not disclosed. Where a company has outside directors/statutory auditors, the total amount of the compensation paid to them and the number of such outside directors/statutory auditors must also be disclosed.

Further, a listed company is required to disclose its basic policy, if any, on the determination of the compensation of each director, statutory auditor and other officer. Unless the specific amount of compensation for each director is stated in the articles of incorporation or approved at a shareholder meeting (which is a rare case in practice), the policy as to how to determine the specific

amount of compensation of each director also needs to be disclosed. If the compensation is linked to performance, the KPIs used for the calculation of the amount of such compensation, the reasons for choosing such KPIs or other prescribed details must also be disclosed.

Furthermore, a listed company is required to disclose the compensation of individual directors, statutory auditors and other officers in its annual securities report under the FIEA if the amount of such individual compensation is JPY100 million or more.

In the case of a closely held company, while there is no such disclosure requirement, its financial statements may have to make available the total amount of compensation paid to its directors, statutory auditors and other officers.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Shareholders, through their ownership of shares, have equity interests in a joint stock company. The basic and primary rights of shareholders are:

- the right to receive dividends;
- the voting right at shareholder meetings; and
- the right to receive residual assets upon the liquidation of the company.

Shares are issued only upon the full payment of the issuance price by a shareholder; accordingly, there exists no obligation of shareholders to make an additional investment/payment in their capacity as shareholders. Additionally, unlike in some other jurisdictions, it is generally construed that a controlling shareholder does not

owe any fiduciary duty in relation to the operation of the company.

Accordingly, in principle, the risk assumed by shareholders is limited to the equity amount invested in the company. However, in limited circumstances, a doctrine to pierce the corporate veil exists pursuant to court precedent where the benefit of the corporate form is abused or the existence of the corporate form becomes a mere facade.

While there is no publicly available record of the shareholders of a company, a shareholder or a creditor of a company can request inspection of the shareholders register that the company is required to keep under the Companies Act.

5.2 Role of Shareholders in Company Management

Shareholders are not directly involved in the management of a company.

Rather, shareholders, in their capacity as members of a shareholder meeting, vote on agenda items presented at the shareholder meeting and make resolutions on such proposed matters. In the case of a company with a board of directors, the shareholder meeting only has the power to make resolutions on the matters stipulated by law or stipulated in the articles of incorporation. Accordingly, it is not expected that a shareholder meeting will make resolutions regarding the day-to-day management of the company.

Once a resolution is passed by a shareholder meeting, the directors of the company owe a duty to act in accordance with such a resolution.

In the case that a director or a company is to take certain actions that are likely to adversely affect shareholders or the company, under limited cir-

cumstances satisfying the criteria stipulated in the Companies Act, a shareholder may demand that the company or director refrain from taking such actions. Additionally, a shareholder may bring a claim against the company or directors as explained in **5.4 Shareholder Claims**.

For the purpose of monitoring the company's management, when satisfying the requirements provided under the Companies Act:

- a shareholder holding 3% or more of the voting rights may request the court to appoint an inspector for the company's business;
- a shareholder holding 3% or more of the voting rights may request the disclosure of the accounting books and related documents of the company; and
- a shareholder may request, with the court's permission, the disclosure of the minutes of meetings of the board of directors.

5.3 Shareholder Meetings

Types of Shareholder Meetings

A company is required to have an annual shareholder meeting once every fiscal year. At an annual shareholder meeting, the financial statements/business reports are approved or reported and annual dividends may be declared. The appointment of directors or statutory auditors may also take place.

The articles of incorporation usually set forth that the shareholders as of the end of the relevant fiscal year will have voting rights at the annual shareholder meeting, and this annual shareholder meeting is required to be held within three months after the end of the relevant fiscal year.

An extraordinary shareholder meeting may be convened from time to time. For a company whose shares may be transferred without restric-

tion (including listed companies), the company must set a record date by giving public notice in order to identify the shareholders who may exercise their voting rights at the relevant shareholder meeting.

Some listed companies are holding a virtual or semi-virtual shareholder meeting by using web conference systems. An amendment to the relevant laws was passed in 2021 that enables a company to have “full” virtual shareholder meeting (ie, a shareholder meeting without a concept of the “venue” of the meeting).

Convocation Procedure

The convocation of a shareholder meeting by the company is required to be made by a resolution of the board of directors and, in general, a convocation notice is required to be sent out to the shareholders at least two weeks prior to the scheduled date of the shareholder meeting.

In the case of a listed company, the required content of the proxy statements for a shareholder meeting is stipulated in the relevant regulations. From the year 2023, pursuant to the latest amendment to the Companies Act, which was enforced on 1 September 2022, a listed company is required to provide the proxy statements via electronic means at least three weeks prior to the scheduled date of the shareholder meeting. In exchange, it is not legally required to send the proxy statements in printed form unless requested so by a shareholder.

In the case of a closely held company with a limited number of shareholders, if all the shareholders agree to have a shareholder meeting with a shortened notice period, a shareholder meeting may be validly held in accordance with such agreement. Additionally, if all the shareholders approve the proposed agenda unanimously in

writing (or by email), then the resolution of a shareholder meeting will be deemed to have been made without having an actual physical meeting.

Apart from the convocation of a shareholder meeting by the company, a shareholder holding 3% or more of the voting rights may, with the court's permission, convene a shareholder meeting.

Proposal by a Shareholder

When the company convenes a shareholder meeting, within the scope of an agenda item proposed by the company, a shareholder may make a counter proposal during the meeting. For example, if the company proposes one individual as a director candidate, a shareholder may make a counter proposal to make another individual a director candidate during the meeting.

Further, a shareholder holding 1% or more of the voting rights (or holding 300 or more voting rights) may request the company add a certain agenda item for an upcoming shareholder meeting by making the request eight weeks prior to the scheduled date of the shareholder meeting.

Resolution Requirement

The voting/quorum requirements for a shareholder meeting resolution differ depending on the agenda item to be resolved.

A super-majority vote, requiring two thirds or more of the affirmative votes among the shareholders present at the meeting, is required for some important matters such as amendments of the articles of incorporation, approval of mergers, dissolution of the company, and others. The quorum requirement, which is the attendance of shareholders holding more than half of all the

voting rights, may be relaxed by the articles of incorporation.

A simple majority vote, requiring more than half of the affirmative votes among the shareholders present at the meeting, applies to general matters such as the approval of financial statements, distribution of dividends, appointments of directors or statutory auditors, and others. The quorum requirement is the attendance of shareholders holding more than half of all the voting rights, which may be relaxed by the articles of incorporation.

There are some other resolution requirements for certain exceptional matters.

Disclosure of Result of Resolution

In the case of a listed company, the voting results for each agenda item (ie, the number of affirmative votes, negative votes and abstentions) are required to be disclosed to the public.

5.4 Shareholder Claims

A shareholder has the right to request the company institute a suit against a director by itself seeking indemnification of the company by the director (or statutory auditors or an accounting auditor). If the company does not bring such a suit by itself within 60 days of the demand being made by the shareholder, the shareholder may, on behalf of the company, bring a suit (a derivative suit) against the director (or statutory auditors or an accounting auditor). In limited circumstances satisfying the requirements under the Companies Act, a shareholder may also bring a derivative suit against the directors (or statutory auditors or an accounting auditor) of a wholly owned subsidiary.

A shareholder may also file an action with the court to nullify certain corporate actions taken

by the company, such as the issuance of new shares, merger, company split and resolution of a shareholder meeting, if there exist grounds for such nullification.

5.5 Disclosure by Shareholders in Publicly Traded Companies

For publicly traded companies, a bulk shareholding report system exists. A shareholder holding more than 5% of the outstanding shares, as calculated pursuant to the relevant regulations, is required to file a bulk shareholding report within five business days of it satisfying such requirements. Thereafter, as long as the shareholder satisfies the requirements, the shareholder is required to file updated reports when material changes occur with respect to the information contained in the report, including the case of an increase or decrease of 1% or more in the shareholding ratio. In this regard, some beneficial owners satisfying the criteria stipulated in the FIEA are deemed to hold the relevant shares, but such regulation is not necessarily able to capture the ultimate beneficial owners.

In the case of institutional investors, some exceptions exist to relax the reporting timing and reduce the reporting contents.

The Council of Experts on the Stewardship Code, established by the Japanese Financial Services Agency, published “*Japan’s Stewardship Code*”. This Code is not a law or a legally binding regulation, but many institutional investors have accepted it and make disclosure in accordance with it. Under the Code, institutional investors should have a clear policy on voting and publicly disclose the same. Additionally, under the Code, institutional investors are expected to disclose voting records, including reasons for their voting decisions, for each investee company on an individual agenda item basis. In relation to dis-

closure/identification of beneficial owners of the shares held by institutional investors, amendment to the Stewardship Code and amendment to the Companies Act are now being discussed.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

The Companies Act provides for annual financial reporting requirements for all joint stock companies. Following the end of each fiscal year, a joint stock company is required to prepare:

- financial statements (consisting of a balance sheet, profit and loss statement, statement of changes in shareholders’ equity, and notes to financial statements);
- a business report; and
- supplementary statements to each of the foregoing.

When finalised, the financial statements and business report will ultimately be submitted to the company’s annual shareholder meeting for either approval or report to the shareholders.

Depending on the governance structure of the relevant joint stock company, the procedural requirements for finalising such documents will vary. In the case of a company with a board of directors, which is the most typical structure, its financial statements, business report and supplementary statements must be reviewed by the company’s statutory auditor or a board of statutory auditors (as applicable), and the financial statements and their supplementary statements must be reviewed and audited by the company’s accounting auditor (if applicable). The board of directors will then approve such documents, which will be approved by the shareholders, or

reported to the shareholders (in the case where the company's accounting auditor has issued an unqualified opinion as to the company's financial statements and other conditions are met), at annual shareholder meetings.

Requirements Under the FIEA

Publicly traded companies (in this context, listed companies and other companies that are required to file annual securities reports under the FIEA) are required to prepare consolidated financial statements as well. In addition, under the FIEA, a publicly traded company is required to submit an annual securities report, which must contain audited financial statements (consolidated and non-consolidated) and be filed within three months of the fiscal year end. A publicly traded company is also required to submit a semi-annual report, which contains summary financial information and must be filed within 45 days of the semi-annual end. Financial information contained in semi-annual reports is required to undergo semi-annual review by the accounting auditor.

Requirements Under the Stock Exchange

With a view to providing more timely financial information to public shareholders, the TSE Regulations also require that Japanese listed companies publish annual and quarterly summaries of consolidated financial results. Accounting auditors' review of financial information contained in such summaries is voluntary subject to certain exceptions. The Tokyo stock exchange requests that such summaries be made public within 45 days of the quarterly end.

6.2 Disclosure of Corporate Governance Arrangements

Corporate governance arrangements are generally required to be disclosed in business reports. Matters to be disclosed include:

- a summary of the company's corporate governance system, internal audit and statutory audit system, outside directors and statutory auditors and their relationships with the company; and
- details regarding compensation, corporate indemnification and D&O insurance.

Publicly traded companies also need to disclose in annual securities reports certain information regarding corporate governance.

In addition, the TSE Regulations require that each listed company submit a corporate governance report based on the Corporate Governance Code. In the corporate governance report, each listed company must explain, among other matters:

- its basic policy on matters included in the Corporate Governance Code established by the Tokyo stock exchange;
- the reasons for non-compliance with any of the principles of the Corporate Governance Code (if applicable);
- any disclosures required under the Corporate Governance Code;
- the composition of shareholders (eg, foreign shareholders, top ten largest shareholders, controlling shareholders, if any);
- the measures for protection of minority shareholders and group management policy where a listed company has a listed subsidiary, parent company, listed downstream affiliate, or upstream affiliate;
- its corporate governance system, including appointment of outside directors;
- the initiatives with respect to shareholders or other stakeholders; and
- its internal control system.

The Corporate Governance Code recommends that companies listed on the Prime Market provide English-language versions of key disclosure documents.

6.3 Companies Registry Filings

A joint stock company is required to file certain matters in a commercial registry, which is administered by the legal affairs bureau, upon incorporation and whenever any change to such matters arises. Matters required to be so registered include:

- corporate name, business purposes, amount of paid-in capital, the class and number of shares;
- the type and number of stock acquisition rights;
- directors, statutory auditors, accounting auditor, branch manager and other statutory organs;
- branches;
- merger, demerger and other statutory reorganisations; and
- dissolution and liquidation.

Matters registered in the commercial registry are publicly available, while the filings made to the legal affairs bureau are not. The legal affairs bureau is tasked with review of the application to confirm if the filings comply with the statutory requirements for the matters required to be registered and it may reject the application if the statutory requirements are not satisfied.

A failure to file a required commercial registry may result in a civil penalty not exceeding JPY1 million.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The following categories of joint stock companies must appoint an accounting auditor:

- a large-sized company (*daigaisha*);
- a company with an audit and supervisory committee; and
- a company with nominating and other committees.

An accounting auditor must be appointed from among external auditing firms or licensed accountants. For publicly traded companies, the accounting auditor usually provides audit certification on the financial statements filed under the FIEA.

In order to ensure independence of an accounting auditor, the Companies Act bars interested firms or persons with ties to the company from serving as an accounting auditor. Also, with the aim of shielding an accounting auditor from undue influence from the management, the board of statutory auditors (or their equivalent), rather than the board of directors, has the right to approve the appointment, removal and compensation of the accounting auditor.

With respect to an accounting audit for a listed company, a statutory registration system is in place where the Japanese Institute of Certified Public Accountants assesses the appropriateness of an external auditing firm, etc, that engages in an accounting audit.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The Companies Act requires any large-sized company (*daigaisha*), any company with an audit

and supervisory committee and any company with nominating and other committees to determine and establish its internal control system to ensure that the company and its corporate group operate in a compliant and appropriate manner. In the case of a company with a board of directors, the board must decide the basic framework of the internal control system to be established. The establishment and implementation of an appropriate internal control system are generally considered to form part of the duties of due care of directors.

A joint stock company is required to outline the decisions made by the board of directors with respect to its internal control system and the implementation of the internal control system in its annual business report. The internal control system is audited by statutory auditors and the board of statutory auditors. Under the TSE Regulations, each listed company must describe its basic policy and implementation status of the internal control system in a corporate governance report as well.

Trends and Developments

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Anderson Mori & Tomotsune (AMT) is one of the largest full-service law firms in Japan, with more than 680 lawyers. It is headquartered in Tokyo, with branch offices in Osaka and Nagoya, and overseas offices in Beijing, Shanghai, Singapore, Hanoi, Ho Chi Minh City, Bangkok and Brussels. AMT has also established associated firms in Jakarta, Hong Kong and London. The firm's combined resources and network provide an extraordinarily powerful value proposition,

enabling it to advise on some of the largest and most complex cross-sector transactions. AMT regularly advises listed companies and investors on corporate governance. Recently, it has advised listed companies on shareholder proposals, including the countermeasures available against proposals from activist funds or disputing shareholders, and subsequent proxy fights.

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JAPAN TRENDS AND DEVELOPMENTS

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Introduction

Following on from 2024, activist investors show no signs of slowing down in Japan as 2025 unfolds, with a variety of approaches being taken towards listed companies, ranging from behind-the-scenes requests for interviews, public campaigns using white papers, exercise of shareholder proposal rights, demand for convocation of shareholders' meetings, and even making acquisition proposals. As a result, facing activists in the correct way has emerged as an urgent imperative for listed companies.

Activists, however, are often not the shareholders listed in the shareholder register (the statutory document in which to check who the current shareholders are under Japanese law) – that is, those who are listed in the shareholder register are nominal shareholders, such as asset management banks that are entrusted by activists to manage the activists' shareholder rights. It has been pointed out that it is difficult for a company to identify those who are behind the nominal shareholder as beneficial shareholders, holding the authority for giving instructions on, for example, the exercise of voting rights. In practice, companies have no viable alternative but to request an investigation from trust banks or other specialised institutions to determine their beneficial shareholders, imposing costs and burdens on listed companies. In response to this, the Financial Services Agency now plans to revise the Stewardship Code to include provisions that, among others, require institutional investors to explain the scale of their shareholdings in the investee company when requested by the investee company.

In addition, based on similar concerns, discussions are underway in relation to an amendment to the Companies Act, which highlights the establishment of a system allowing for the

identification of beneficial shareholders. On 10 February 2025, the Minister of Justice consulted the Legislative Council on the revision of the Companies Act. While the deliberations at the Legislative Council Subcommittee on the Companies Act are set to continue, in February 2025, the Japan Institute of Business Law (the “*Institute*”) moved ahead by releasing its “*Report of the Study Group on Companies Act Legislation*”. Given that the report will serve as a starting point for the forthcoming deliberations at the Legislative Council on the potential amendment to the Companies Act and offers a valuable insight into what direction the amendment might actually take, details of the report are introduced below in “*Outline of the Report of the Study Group on Companies Act Legislation*”.

In response to the Guidelines for Corporate Takeovers (the “*Guidelines*”) published by the Ministry of Economy, Trade and Industry (METI) in August 2023, the number of cases of so-called “*acquisitions without consent*” continues to grow. The Guidelines were formulated following discussions by the council of experts established at the METI with the purpose of presenting principles and best practices that should be shared throughout the economy to develop fair rules regarding M&A transactions, with a focus on how parties should behave in the context of acquiring corporate control of a listed company, and they have greatly affected the board of directors' code of conduct in M&A transactions.

One of the most notable impacts the Guidelines have had on the Japanese market has been the increase in acquisitions without consent. (An acquisition without consent is one that is conducted without prior consultation with the target company. Formerly known as “*hostile takeover*” or “*hostile acquisition*”, the Guidelines proposed renaming it as an acquisition without consent

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since it is not necessarily hostile, and the new term quickly gained widespread traction after the Guidelines were established.) The Guidelines provide that, even in the absence of prior approval of the target company, the latter's board of directors must give proper consideration to a deal proposal if a bona fide offer has been made. Since the publication of the Guidelines, acquisitions without consent have also been on the rise in Japan, but what stands out the most in the recent trend is the proposal for acquisitions without consent from non-Japanese companies targeting corporate giants representing Japan. The evolving landscape carries significant implications from a corporate governance perspective for directors and other officers of listed companies, as it demands them to steer their organisations with heightened urgency in anticipation of potential acquisition proposals from foreign players of considerable scale and financial strength.

Outline of the Report of the Study Group on Companies Act Legislation

The Institute has discussed various issues including:

- the free distribution of shares to employees;
- revisions to the share distribution system;
- revisions to the regulations on in-kind contributions, virtual shareholders' meetings and virtual bondholders' meetings;
- revisions to the requirements for the number of voting rights for shareholder proposals;
- revisions to the system for companies with nominating committees and other committees; and
- revisions to the liability of officers.

The following, however, presents an outline of the deliberations regarding the establishment of a system allowing for the identification of benefi-

cial shareholders, which is deemed the highlight of the proposed amendments to the Companies Act and which is considered to deserve attention in the context of corporate governance.

Establishment of a system allowing for the identification of beneficial shareholders *Background*

Under the current system, except where the large shareholding reporting system applies (ie, shareholding over 5%), there is no system in place for stock companies or other shareholders to identify those who are behind the nominal shareholders, holding the authority for giving instructions on, for example, the exercise of voting rights. In recent years, while it has been regarded as important for stock companies to promote constructive dialogue with their shareholders in order to increase corporate value over the medium to long term, in light of cases where a nominal shareholder is not always the best counterpart for a dialogue (such as cases where those who hold the authority to instruct on the exercise of voting rights are hiding behind the nominal shareholder), the report indicated the directionality to consider the establishment of a system under the Companies Act that enables stock companies to identify the so-called beneficial shareholders, thereby promoting constructive dialogue between the stock companies and their shareholders.

Meanwhile, the report also raises the possibility of framing the system's purpose not only as the promotion of constructive dialogue between stock companies and their shareholders, but also as the protection of the common interests of shareholders. To be specific, the report positions the system as a means to promote dialogue between stock companies and their shareholders, and at the same time a safeguard

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against scenarios in which, for example, multiple unidentified investors virtually buy up the shares behind the backs of nominal shareholders, refuse to engage in dialogue with the company, and instruct their nominal shareholders to exercise their voting rights, ultimately undermining the common interests of shareholders.

Details of the specific system

The following proposals are under consideration, and discussions within the Institution revealed divergence of opinions for each option.

- *Proposal A* – Stock companies are entitled to request a shareholder listed in the shareholder register to provide information as to whether or not there is a beneficial shareholder and, if so, to provide relevant information about such beneficial shareholder, and the shareholder who is so requested must provide such information within a specified period. Furthermore, the stock company may request the beneficial shareholder to provide information as to whether or not there is a further beneficial shareholder and, if so, to provide information about such ultimate beneficial shareholder, and the beneficial shareholder who is so requested must provide such information within a specified period. Those who fail to provide the information or provide false information will be subject to a civil fine.

This proposal aims to have the system allow for the identification of beneficial shareholders through the promotion of dialogue between stock companies and their shareholders, and attempts to design the system only to the extent necessary to achieve this purpose.

- *Proposal B* – Proposal B is largely the same as Proposal A above, but goes further, restricting the voting rights of those who fail to provide information or who provide false information at the next shareholders' meeting held after the date on which the stock company requested them to provide information (Proposal B-1). A derivative of Proposal B-1 (Proposal B-2) follows the same approach as Proposal A in imposing a civil fine on those who fail to provide information or provide false information, but further states that the stock company can restrict their voting rights from being exercised at the next shareholders' meeting if the exercise of voting rights by such nominal shareholders and the equivalent is deemed to significantly undermine the common interests of shareholders.

While these proposals build on Proposal A, they establish rules to restrict the voting rights of those who fail to provide relevant information on beneficial shareholders, in order to ensure effectiveness.

- *Proposal C* – An obligation is imposed on stock companies to investigate relevant information on beneficial shareholders, incorporate such information into the shareholder register and make it available for disclosure through the inspection of the shareholder register. On top of this, the voting rights of those who fail to provide relevant information on beneficial shareholders are restricted, while at the same time those who are listed or recorded in the shareholder register as the holders of the authority for giving instructions are permitted to directly exercise their voting rights (including attending the shareholders' meetings to propose agendas or to request explanations on specific matters) and other rights attached to the shares.

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What is most difficult about this proposal is whether it is appropriate to impose an obligation on stock companies to investigate relevant information on beneficial shareholders.

Issues to consider

While, as noted above, the purpose of the system remains a matter of debate, other issues to consider in establishing the system as raised by the report and the outline of deliberations within the Institution over such issues, are as follows.

- *Scope of companies subject to the system* – not to mention listed companies, should the system also apply to non-listed companies, in light of the purpose of the system?

At the deliberation, there were opinions expressing support for the system to apply to non-listed companies too, as the need for a dialogue between the company and its shareholders may occur for non-listed companies as well. On the other hand, there were also opinions expressing that the suspension of voting rights could be an excessive regulation if there is no need for it, and there should be investigation into whether there is a need for such regulation with non-listed companies.

- *Meaning of “beneficial shareholders”* – should “beneficial shareholders” mean “those who have the authority to instruct on the exercise of voting rights that are attached to the shares” or should the definition also pay attention to rights beyond voting rights, such as rights to dispose of shares?

At the deliberation, opinions focusing on the voting rights of shareholders suggested that “beneficial shareholders” means “those who have the authority to instruct on the exercise of voting

rights that are attached to shares”. On the other hand, there were opinions expressing that “beneficial shareholders” should cover investors who are: instructing on the policy for exercising voting rights; expressing their ex post facto opinion over or giving retrospective criticism on the exercise of voting rights; giving consents for exercising the voting rights; and receiving reports on the results of exercising the voting rights.

- *Mechanism for companies to identify beneficial shareholders* – is it sufficient for the system to allow for stock companies to request that the nominal shareholders provide relevant information on beneficial shareholders, or should the system place the nominal shareholders under an obligation to investigate the ultimate authority holding the right to give instructions, and, thereupon, impose further obligation to provide the results of such investigation to the stock company?

At the deliberation, while some opinions expressed the view that it would be sufficient to allow for stock companies to request that the nominal shareholders provide relevant information on beneficial shareholders, others pointed out the burden on stock companies having to individually request information from each authority holding the right to give instructions in order to identify the beneficial shareholder, as well as concerns regarding the practical usability of the system.

- *Scope of relevant information on beneficial shareholders that stock companies are entitled to request* – is it sufficient for the system to allow for stock companies to request information necessary to identify the beneficial shareholder (ie, (i) full name of the individual or name of the entity, and (ii) address and other contact information) as well as the number

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of shares in which such beneficial shareholder holds the authority?

Opinions expressed at the deliberation supported the view that the scope of information is sufficient if it covers: (A) (i) the full name of the individual or name of the entity, and (ii) address and other contact information; and (B) the number of shares in which the beneficial shareholder holds the authority. There were no opinions requesting to add any other information.

- *Disclosure of provided information* – in light of the purpose of the system, allowing for stock companies to identify information on their beneficial shareholders should be sufficient, so is it necessary to disclose the information to other shareholders or to the public?

Many opinions expressed at the deliberation agreed that allowing for stock companies to identify information on their beneficial shareholders should be sufficient, and it was pointed out that disclosing such information could cause violent fluctuation of stock prices or other unnecessary confusion in the market.

- *Sanctions for failure to provide information* – in addition to civil fines, should restrictions be imposed on the exercise of voting rights, and if so, how should such restrictions be imposed?

This was the most intensely debated issue at the deliberation, and diverse opinions were expressed. From the perspective of ensuring effectiveness, several opinions expressed that civil fines alone are weak and insufficient as a sanction and that restrictions on the exercise of voting rights are necessary. On the other hand, concerns were raised for Proposal B that imposing restrictions on the exercise of voting rights

could lead to legal instability, such as the possibility of grounds for rescinding the resolution of the shareholders' meeting being found. In particular, opinions regarding Proposal B-2 pointed out that: the requirement of "*if it is deemed to significantly undermine the common interests of shareholders*" is too abstract and thus even more unstable; the requirement is too stringent; and the framework "*allowing*" for the stock company to restrict the exercise of voting rights is problematic in the sense that it could permit arbitrary treatment by the company. It was also pointed out that, regarding the restrictions on the exercise of voting rights, it is appropriate to require judicial review as a condition for suspending voting rights. Additionally, as to civil fines, it was noted that while a civil fine seems sufficient if premised solely on the purpose of the system, that is, to promote dialogue between companies and their shareholders, imposing a civil fine on an individual shareholder would be unprecedented.

Trends in Acquisitions Without Consent

The Guidelines were formulated with the purpose of presenting principles and best practices that should be shared throughout the economy to develop fair rules regarding M&A transactions, and includes acquisitions without consent within their scope. According to the Guidelines, generally, upon receiving a proposal containing a specific acquisition offer that seeks to gain control over the management of a company, including an offer of acquisition without consent, the offer must be submitted to the target company's board of directors for deliberation, and the directors and the board of directors (including, if applicable, the special committee established by the target company) should determine whether the acquisition proposal will increase the company's corporate value, and make reasonable efforts to ensure that the acquisition is

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conducted under terms and conditions which benefit ordinary shareholders.

A landmark year for M&A in Japan, 2024 saw an unprecedented surge in the number of cases of acquisitions without consent. Specific examples include:

- Bain Capital's counterproposal without consent against KKR's tender offer for FUJISOFT (ultimately resulting in KKR's tender offer succeeding);
- Brother Industries' counterproposal without consent against Roland DG's management buyout (ultimately resulting in the management buyout being completed);
- AZ-Com Maruwa Holdings' acquisition proposal without consent for Chilled & Frozen Logistics Holdings (ultimately, SG Holdings, which emerged as a white knight, acquired Chilled & Frozen Logistics Holdings); and
- Nidec's acquisition proposal without consent for Makino Milling Machine (ongoing).

Among these developments, particularly notable cases of overseas companies making an acquisition proposal without consent are those of Alimentation Couche-Tard (ACT) for Seven & i Holdings (Seven & i), and of Yageo Corporation (Yageo) for Shibaura Electronics, which was announced at the start of 2025. The outline of these two cases, based on publicly available sources such as press releases from the respective companies, is as follows.

Case 1: Seven & i

- On 25 July 2024, ACT, without giving prior notice, made a non-binding acquisition proposal to Seven & i at a per share price of USD14.86 per ordinary share.
- On 8 August 2024, following the receipt of the above proposal, Seven & i established a

special committee comprised of its outside directors to review ACT's proposal (based on Seven & i's publications dated 25 March 2025).

- On 6 September 2024, Seven & i released a public announcement stating its opinion that ACT's proposal significantly undervalued the shares of Seven & i and that ACT failed to address regulatory hurdles, particularly issues related to US antitrust laws.
- According to Seven & i's publications dated 25 March 2025, on 19 September 2024, ACT submitted a non-binding revised proposal at a per share price of USD18.19. In the proposal, ACT stated that the US antitrust issues should be resolved through counsel-to-counsel discussions. Thereafter, various discussions regarding the acquisition, including US antitrust issues, have continued between the two companies.
- While the founding family of Seven & i had reportedly considered a management buyout (MBO), Seven & i announced on 27 February 2025 that it had received a notice from the founding family that the necessary funding to make the formal proposal for the MBO could not be secured.

Case 2: Shibaura Electronics

- On 5 February 2025, Yageo announced its intention to conduct a tender offer to acquire the shares of Shibaura Electronics (the proposed commencement date of the tender offer being 7 May 2025). The tender offer price was set at JPY4,300 per share of Shibaura Electronics' common stock.
- On 10 February 2025, Shibaura Electronics announced the establishment of a special committee comprised primarily of its outside directors to review Yageo's proposal. Subsequently, Shibaura Electronics announced that it was engaging in communications with

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Yageo through the exchange of questionnaires and other means.

- On 10 April 2025, MinebeaMitsumi announced its intention to commence a tender offer for Shibaura Electronics (the proposed commencement date of the tender offer was 23 April 2025). The tender offer price was set at JPY4,500 per share of Shibaura Electronics' common stock, exceeding Yageo's proposal. In response, Shibaura Electronics announced its opinion in support of MinebeaMitsumi's tender offer and its opinion opposing Yageo's tender offer.
- On 17 April 2025, Shibaura Electronics announced that it had received a proposal from Yageo to increase the tender offer price for the planned tender offer to JPY5,400.
- On 1 May 2025, MinebeaMitsumi announced that it would increase the tender offer price to JPY5,500 and commence the tender offer process from 2 May 2025. On the same day, Shibaura Electronics announced that it would maintain its opinion to support MinebeaMitsumi's tender offer and recommend its shareholders to tender their shares to such tender offer.
- On 8 May 2025, Yageo announced that it would increase the tender offer price to JPY6,200 and commence the tender offer process from 9 May 2025.
- On 21 May 2025, Shibaura Electronics announced that (i) it would reserve its opinion in relation to Yageo's tender offer (changing its previous position of opposing such tender offer) and (ii) it would withdraw its opinion to recommend its shareholders to tender their shares to MinebeaMitsumi's tender offer while

its opinion to support such tender offer was still maintained.

- As of the date of publication of this guide (17 June 2025), Shibaura Electronics is currently reviewing the proposal from Yageo while also approaching MinebeaMitsumi regarding whether they have any intention to change the price for their tender offer.

Significance of Cases 1 and 2

What is groundbreaking about the above two cases is that both involved proposals for acquisition without consent by overseas companies. Acquisitions without consent by overseas players in the past were assumed to have been discussed behind the scenes, but they are now becoming a realistic possibility for Japanese companies. In particular, the fact that even a corporate giant like Seven & i, one of Japan's most prominent flagship companies with a market capitalisation of several trillion yen, could become a target of an acquisition without consent has come as a surprise to Japanese society. The emergence of these cases marks the beginning of a new phase in the practical implementation of acquisitions without consent in Japan, and directors of Japanese companies are increasingly required to consider proposals for acquisitions without consent as a realistic possibility and manage their businesses accordingly. Furthermore, in the event that a proposal regarding an acquisition without consent is received, directors of Japanese companies must conduct a sincere review in accordance with the Guidelines, with an emphasis on the enhancement of corporate value and the interests of shareholders.

KENYA

Law and Practice

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Kieti Law LLP is a leading Nairobi-based law firm specialising in corporate law and finance, operating under Cliffe Dekker Hofmeyr's umbrella. They offer a comprehensive and responsive approach, tailoring their services to meet clients' legal needs. The firm boasts a team of experienced and versatile financing lawyers with a strong reputation for exceptional service. They excel at handling complex deals and regularly advise leading Kenyan and international corporations, financial institutions, and govern-

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Kenyan law provides diverse legal structures to accommodate various specific needs.

Companies

The most common form of corporate organisation is a company. The Companies Act, Chapter 486 of the Laws of Kenya ("*Companies Act*") provides for the following types of companies:

Companies limited by shares

A company is limited by shares if the liability of its members is limited by the company's articles to any amount unpaid on the shares held by the members. A company limited by shares can take one of two forms.

Private limited companies

Companies whose articles restrict a member's right to transfer shares, limit membership to 50, prohibit public invitations to subscribe for shares or debentures of the company and require all members to consent to add a new member.

Public limited companies

Companies whose articles allow their members the right to transfer their shares in the company and do not prohibit initiations to the public to subscribe for shares or debentures of the company.

Companies limited by guarantee

A guarantee limits a company if its articles limit its members' liability to the amount they undertake to contribute to the company's assets in the event of its liquidation, and its certificate of incorporation states that it is limited by guarantee.

Unlimited companies

A company is unlimited if there is no limit on the liability of its members, and its certificate of incorporation states that the liability of its members is unlimited.

Partnerships

Kenya also recognises various partnership structures. These are set out below.

General partnerships

A partnership is a relationship between persons carrying on a business in common and seeking profit. This traditional model entails unlimited liability for all partners, who share full responsibility for the partnership's operations. They can:

- sue and be sued in their own name;
- enter contracts and own property for business purposes; and
- ensure continuity despite partner changes, subject to the partnership agreement.

Limited partnerships

A form of partnership recognised as a limited partnership involves:

- at least one general partner with unlimited liability and responsibility for the management of the limited partnership's business; and
- one or more limited partners whose liability is restricted to their initial contribution to the partnership.

Limited liability partnerships (LLPs)

LLPs combine features of general partnerships with limited liability benefits typically associated with companies. Upon registration, LLPs become a separate legal entity with perpetual succession. As such, an LLP:

- is a legal entity separate from its members;

- has unlimited capacity and can do anything that a legal person can do; and
- its members have limited liability; hence, they do not need to meet the LLP's liabilities.

1.2 Sources of Corporate Governance Requirements

Several key sources that establish corporate governance requirements for companies in Kenya have been outlined below.

- The Companies Act sets out the primary legal framework governing the formation, operation, and dissolution of companies, including aspects of corporate governance.
- The Insolvency Act, Chapter 53 of the Laws of Kenya ("*Insolvency Act*"), provides regulations for dealing with financially distressed companies and influences how companies manage their finances.
- The Partnership Act, Chapter 29 of the Laws of Kenya ("*Partnership Act*"), sets out the framework for the formation, management and operation of general partnerships and limited partnerships.
- The Limited Liability Partnerships Act, Chapter 30 of the Laws of Kenya ("*LLP Act*") specifically addresses the registration and management of LLPs.
- Common law: Principles established through past court decisions (precedent) in England regarding companies can still be relevant even if not directly codified in Kenyan law.
- Internal governance documents: A company's articles of association or a partnership's partnership deed and, in the case of companies listed on the Nairobi Securities Exchange ("*NSE*"), its board charter, establish internal rules regarding its operations, including director powers and shareholder meetings.
- The Code of Corporate Governance Practices for Issuers of Securities to the Public,

2015 (the "*CMA Governance Code*") is a set of guidelines issued by the Capital Markets Authority ("*CMA*") that apply to publicly traded companies in Kenya and sets out various requirements aimed at ensuring fair treatment of shareholders, transparency, and responsible management.

- The Code of Governance for State Corporations (*Mwongozo*) is a set of guidelines that lays a foundation for the management, governance and oversight of state corporations in Kenya.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Publicly traded companies in Kenya must comply with the CMA Governance Code. Some key requirements have been outlined below.

Fair Treatment of Shareholders

The CMA Corporate Governance mandates companies to treat all shareholders fairly, including minority and foreign shareholders. This includes ensuring equal voting rights and access to information.

Disclosure

The CMA Governance Code follows an "*Apply or Explain*" principle in which listed companies must fully disclose any instances where they are not complying with the CMA Governance Code. While the CMA may consider satisfactory explanations for non-compliance, adherence to the mandatory disclosure provisions outlined in the Capital Markets (Public Offers, Listing and Disclosures) Regulations, 2023 ("*Disclosure Regulations*") is essential.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

The Kenyan corporate governance landscape is witnessing an increased focus on environmental and social responsibility. This emphasis is particularly evident in the realm of “green” and sustainability reporting.

In this regard, the Central Bank of Kenya (“CBK”) published the Guidance on Climate-Related Risk Management (“*CBK Guidance*”), which lays out a framework for banks and mortgage refinance companies, requiring them to integrate climate-related risks into their core functioning and ensuring that business decisions and activities account for potential climate impacts.

Key Aspects of CBK Guidance

Time-bound plans

Banks and mortgage refinance companies must develop a concrete plan with specific timelines. This plan, detailing the implementation of the CBK guidance, needs approval from the board and signatures from both the CEO and Chairman.

Quarterly reporting

To ensure accountability, banks and mortgage refinance companies must submit quarterly progress reports to the CBK within ten days after the end of each calendar quarter, starting from 30 September 2022.

Future impact

The emphasis on climate-related risk management by the CBK strongly suggests that “green” and sustainability reporting will be a major talking point in Kenyan corporate governance for 2023 and the foreseeable future. It is likely to extend to other players in the financial sector and influ-

ence corporate governance practices across a broader spectrum of Kenyan businesses.

2.2 ESG Considerations

There are no requirements for private or public companies to report on ESG issues. However, companies listed on the NSE have the following reporting requirements.

Companies Act

The directors’ report for listed companies must incorporate a business review section. This section delves into the company’s environmental practices, employee treatment, and social and community involvement.

NSE ESG Disclosures Guidance Manual (“ESG Manual”)

Issued in late 2021, this manual provides listed companies with a framework for collecting, analysing, and publicly disclosing ESG information. The objective is to achieve alignment with internationally recognised reporting standards.

Sustainable Finance Initiative

In addition, certain industries, such as the banking sector, have established their own ESG-related guidelines. For instance, the Kenya Bankers Association’s Sustainable Finance Initiative (“SFI”) encourages its member banks to:

- implement robust environmental and social risk management systems; and
- publish comprehensive sustainability reports biennially (every two years).

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies and functions involved in the governance and management of a company in Kenya are the board of directors, the company secretary, the shareholders and the contact person.

Board of Directors

The board of directors is ultimately responsible for overseeing the company's affairs. As stipulated by the Companies Act, the directors are entrusted with the power to direct and regulate the company's business, set strategic direction, and ensure compliance.

While the board of directors retains ultimate authority, it can delegate specific functions to individual directors, committees, management teams, and employees.

Company Secretary

The Companies Act mandates that public and private companies with a share capital of KES5,000,000 (approximately USD38,760) or more appoint a company secretary.

The company secretary has various responsibilities, including documenting board and shareholder meetings and maintaining registers of directors, shareholders, and debenture holders. They also liaise with the Registrar of Companies and file required documents like annual returns and financial statements.

Shareholders

Shareholders are the company's owners. Their ownership translates into specific rights and influence over the company's direction. Shareholders exercise their power through voting

rights, allowing them to elect board members and approve significant changes, including amendments to the company's articles of association.

Contact Person

Private companies or companies limited by guarantee that do not meet the threshold for a company secretary and do not have a resident director in Kenya must appoint a contact person.

The contact person's primary function is to maintain critical company records, including those related to directorships, shareholding, beneficial ownership, and any other information required by law. Notably, the contact must be a natural person with a permanent Kenyan residence.

3.2 Decisions Made by Particular Bodies

Directors

The Board of Directors serves as the main decision-making body of the company. It oversees daily operations and establishes the company's strategic direction. Typically, the articles of association state that the company's management is entrusted to the directors, who have the authority to exercise all powers of the company.

Shareholders

Certain fundamental decisions are explicitly reserved for the shareholders and require a formal resolution passed at a duly constituted meeting. These decisions typically involve significant changes to the company's core structure or capital, such as amendments to the articles of association and alterations to the share capital. The company's articles of association may, however, allow for delegating certain reserved decisions to the board of directors.

3.3 Decision-Making Processes

The board of directors and the shareholders make the decisions through the following processes:

Directors

The board makes decisions through formal resolutions, typically reached during board meetings. The company's articles of association outline the specific procedures, quorum requirements (the number of members needed to be present), meeting notice periods, and voting requirements for passing resolutions. Generally, a simple majority vote suffices. Written resolutions can also be used to make decisions without a physical meeting.

Shareholders

Shareholders make decisions through shareholder resolutions. These resolutions can be passed either by a vote at a formal shareholders' meeting or as a written resolution without a meeting. Some exceptions exist, such as the early removal of a director or auditor, which requires a meeting and cannot be done through a written resolution. The type of resolution needed, ordinary (simple majority) or special (75% majority), depends on the specific decision and is dictated by both the Companies Act and the company's articles of association.

4. Directors and Officers

4.1 Board Structure

Number of Directors

Private companies must have at least one natural director, although their governing documents may establish a higher minimum or maximum number.

Public companies, in contrast, must have at least two directors, at least one of whom must be a natural person. Based on their governing documents, public (and private) companies can set a higher minimum or maximum number of directors.

Leadership

In most cases, the board elects a chairperson from its members to lead and manage board meetings unless the company's articles of association or a shareholders agreement specify otherwise.

4.2 Roles of Board Members

The Companies Act provides for a single-tiered board of directors with no distinctions unless a company elects to differentiate certain managerial roles for certain board members. In some cases, the chairperson may be given a casting vote in the event of a deadlock in a decision of the directors. The board of directors is in charge of managing the company's business.

4.3 Board Composition Requirements/Recommendations

The Companies Act does not prescribe the composition of the board of directors for private or unlisted public companies. These entities are free to appoint directors as deemed necessary to fulfil their specific requirements.

However, companies listed on the NSE must ensure their board composition complies with the recommendations outlined in the CMA Governance Code.

Balance of Directors

The board should be comprised of a balanced mix of executive directors responsible for the company's day-to-day operations and non-executive directors who provide independent

oversight and guidance. Most of the directors should be non-executive directors, and one-third of the board should be independent non-executive directors.

Board Size

The optimal size of the board should be determined based on the company's specific needs and operations. It should be large enough to accommodate a diversity of expertise and perspectives yet remain conducive to productive discussions during board meetings.

Director Limits

An individual director of a listed company (excluding corporate directors) cannot hold such a position in more than three publicly listed companies concurrently.

In addition, certain industries, such as banking and insurance, may have additional board composition requirements based on *"fit-and-proper"* assessments conducted by the relevant regulatory bodies on the directors.

4.4 Appointment and Removal of Directors/Officers

Appointment of Directors

The Companies Act allows for appointing directors upon a company's incorporation. This process is set out in the articles of association for future appointments. As such, directors are typically appointed by a resolution of the shareholders, with a simple majority vote sufficing. However, the articles of association may prescribe specific instances where the directors may appoint a director (eg, filling a casual vacancy.)

Restrictions on appointment of directors

The Companies Act limits who can be appointed as a director. Firstly, any individual under the age of eighteen is automatically ineligible. Fur-

thermore, the company's articles of association will ordinarily preclude specific groups of people from acting as directors. Such groups may include undischarged bankrupts and individuals deemed to be of unsound mind. This aligns with the Insolvency Act, which further prohibits undischarged bankrupts from participating in the management or control of any business without the express consent of a bankruptcy trustee or the court.

Removal of Directors

Ordinary resolutions can remove a director. However, specific procedures must be followed. The director in question must receive a special notice detailing the proposed removal. The director is then given the opportunity to submit written representations within twenty-one days of receiving the notice.

Following the receipt of any representations, the board must convene a meeting to consider the matter. The director facing removal is entitled to be heard during this meeting when the motion for removal is being considered. If the motion for removal is passed, the director retains the right to challenge the removal in court.

It is important to note that even after being removed from office, a director remains subject to certain continuing duties. These duties include:

- the obligation to avoid conflicts of interest regarding exploiting any property, information, or opportunity that the individual became aware of while acting as a director; and
- the prohibition on accepting benefits from third parties concerning actions taken or omitted during their tenure as a director.

4.5 Rules/Requirements Concerning Independence of Directors

Independence of Directors

There are no rules and requirements on the independence of directors in private companies or unlisted public companies. On the other hand, listed companies must ensure that at least one-third of the board of directors are independent non-executive directors. Under the CMA Governance Code and the Disclosure Regulations, a director is considered to be independent if he or she:

- is not an executive director;
- does not have a material or pecuniary relationship with the company or related persons;
- is compensated through sitting fees or allowances;
- does not own shares or owns less than 5% of the shares in the listed company; and
- serves in such a role for a maximum period of six years.

Conflict of Interest

The Companies Act requires that a company director avoid any situation where they have, or may potentially have, a direct or indirect interest that conflicts with or could conflict with the company's interests. However, this duty to avoid a conflict of interest is not violated if the other directors have approved the situation in question.

The duty to avoid conflict of interest and not to accept benefits from third parties to survive the cessation from office as a director dictates that if a director has personal interests in proposed or existing transactions with the company, they are required to give notice of such interest to the other directors and, in the case of a public company, to the members of the company within 72 hours. Failure to disclose a personal interest

under the Companies Act is an offence, and on conviction, the director concerned is liable to pay a fine not exceeding KES1,000,000.

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors in Kenya arise from common law and have been codified under the Companies Act. These duties include those listed below.

Acting Within Their Powers

Directors have specific authorities outlined in the company's constitution. These powers must be used solely to benefit the company, not for personal gain or the interests of others and for the specific purpose for which they are conferred.

Promoting the Company's Success

Directors are obligated to make decisions they believe, in good faith, will best promote the company's success for its shareholders. This includes considering long-term consequences, employee interests, community impact, and fostering good relationships. When a company becomes insolvent, the director's primary duty shifts to protecting creditors' interests.

Exercising Independent Judgment

While seeking professional advice is encouraged, directors must ultimately make independent decisions. They cannot mindlessly follow the will of others or rely solely on external advice. However, some situations may require following pre-existing agreements or the company's constitution.

Exercising Reasonable Care and Diligence

Directors are expected to exhibit the same level of care, skill, and diligence as a reasonably competent person. This includes applying their own knowledge and experience alongside any

relevant expertise. Failure to do so could lead to negligence claims against them.

Avoiding Conflicts of Interest

Directors must steer clear of situations where their personal interests conflict or could potentially conflict with the interests of the company. This includes exploiting company property, information, or opportunities for personal gain. This obligation is strict and applies even if the company might benefit from such actions. Violating this duty can lead to severe consequences, including criminal charges. However, it is acceptable to engage in situations that are unlikely to create a conflict of interest.

Not Accepting Benefits from Third Parties

Directors are prohibited from accepting benefits (gifts, bribes, etc) from third parties arising from their position. This includes offers of hospitality intended to influence their decisions. Such actions violate the Companies Act and potentially other anti-bribery laws. However, minor benefits unlikely to create a conflict are permissible. Additionally, benefits from the company itself are not restricted by this duty.

Disclosing Any Interest in Transactions

Directors must declare any direct or indirect interests in company transactions or arrangements. This obligation applies to private and public companies, although the timelines and procedures for disclosure may vary. Failure to disclose such interests or providing inaccurate information can result in penalties. However, directors are not held responsible for conflicts they are unaware of or if their interest is considered insignificant.

4.7 Responsibility/Accountability of Directors

Under Kenyan law, directors primarily owe their duty to the company and not to individual share-

holders or other stakeholders. This principle is codified in the Companies Act.

The company's success is the primary objective of its directors; however, there are circumstances where their responsibilities also include the well-being of other stakeholders. This can encompass employees, customers, and suppliers. For example, promoting the company's success may require directors to consider the effects of their decisions on employees, the community, and the environment. It also involves building strong relationships with suppliers and customers.

In addition, if the company enters insolvency proceedings, the directors' duties shift. The Insolvency Act takes precedence, requiring them to prioritise the interests of creditors and other stakeholders involved in the insolvency process.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Directors owe their primary duty to the company, not to the shareholders. Therefore, acting through its proper organs (usually the board or shareholders in a general meeting), the company is the primary party that can enforce a breach of directors' duties.

However, shareholders have derivative claim rights under Kenyan law. This means that if the company fails to take action for a breach of directors' duties that harms the company, a shareholder can bring a lawsuit against the directors on behalf of the company. The directors' actions ultimately impact the value of the company's shares, which affects shareholders.

Breach of directors' duties in Kenya can lead to several consequences for directors, as outlined below.

- Personal liability – directors can be ordered to pay damages to the company for any losses caused by their breach.
- Accountability for profits – if directors breach their duty by profiting from a conflict of interest, they may be required to return those profits to the company.
- Removal from office – shareholders can remove directors who have breached their duties by voting at a general meeting.
- Disqualification – in serious cases, a court can disqualify a director from holding office in any company for a set period. This can significantly damage a director's career prospects.
- Criminal prosecution – certain breaches of directors' duties may be criminal offences punishable by fines or imprisonment.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Beyond breaches of corporate governance requirements, directors and officers in Kenya can face claims and enforcement actions for various reasons under Kenyan law.

Negligence

Directors and officers must act with reasonable care and skill in managing the company. If their actions or lack thereof cause harm to the company, shareholders, or creditors due to negligence, they can be held personally liable.

Breach of Fiduciary Duty

Directors and officers owe a fiduciary duty to the company, which includes duties of loyalty and good faith. If they act in their interests or those of a third party at the company's expense, they can be liable for the resulting losses.

Misfeasance and/or Breach of Trust

Similar to a breach of fiduciary duty, this applies when directors or officers misuse company

property or assets for personal gain or purposes outside the company's interests.

Statutory Violations

Specific laws such as the Companies Act, the Capital Markets Act or the Competition Act may impose liability on directors and officers for breaches of their provisions.

The Companies Act in Kenya restricts attempts to shield directors and officers from liability. It voids any clause in the company's articles, contracts, or other documents that attempt to exempt directors from liability arising from negligence, default, breach of duty, or breach of trust.

Companies can, however, obtain insurance for directors and officers to cover liabilities incurred while acting in the company's best interests. This insurance wouldn't protect directors from intentional wrongdoing or gross negligence.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Directors' service contracts that extend beyond two years require the approval of company members. This requirement does not apply to companies not registered under the Companies Act or wholly owned subsidiaries of other corporate entities. Where a director's service contract is entered into in contravention of the provisions of the Companies Act, the contract is void to the extent of the contravention, and the company is entitled to terminate the contract with reasonable notice.

4.11 Disclosure of Payments to Directors/Officers

Directors of a company (excluding companies subject to the small companies regime) must include details of the benefits they have received

in that financial year in the notes to the company's individual financial statement.

The directors of a listed company shall prepare a directors' remuneration report for each financial year. A quoted company is one whose equity share capital has been included in the official list on a stock exchange or other regulated market in Kenya.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Individuals become members of a company by subscribing to shares on:

- incorporation;
- the creation of new shares; or
- through a transfer of shares from an existing shareholder.

Shareholders provide equity or financial backing to a company and are generally liable only for the amount of their unpaid shares.

The Companies Act provides that a company's constitution binds the company and its members to the same extent as if the company and its members had covenanted with each other to observe the constitution, making the relationship contractual in nature.

The company's constitution (articles of association) governs the relationship between the company and its members, including the rights attached to the respective members' shares. In some cases, members may opt to enter into a private shareholders agreement to govern the relationship amongst themselves.

Generally, a company is a separate legal entity from its shareholders. This separate personality is not without limits, and courts may allow piercing the corporate veil in cases of fraud and serious misconduct. The concept of piercing the corporate veil is recognised under Kenyan law, and courts will do so if satisfied that there has been serious misconduct or fraud. In doing so, the individuals behind the company who have committed a wrong using the company will be held personally liable.

The Companies Act requires a company to maintain a register of its shareholders, including their names, addresses, shareholding details, dates of becoming and ceasing to be shareholders, and any distinctions between classes of shares. The register must be kept at the company's registered office, and a copy must be submitted to the Registrar of Companies. Although the Companies Act does not expressly provide for public access to this information, certain shareholder details may be obtainable through a formal search at the Companies Registry, subject to the applicable fees, including the shareholders' names, addresses, and shareholding details.

5.2 Role of Shareholders in Company Management

Shareholders are not involved in the company's day-to-day running, as this is a function of the board of directors. Shareholders, however, have the power to appoint and remove directors from office. In addition, certain decisions, such as loans by a company to its directors, may only be made with shareholders' approval.

5.3 Shareholder Meetings

Every company must hold an annual general meeting within a year. Failure to do so can result in a fine of up to KES100,000 (approximately USD775).

All private or public companies must provide members with at least 21 days' notice for annual general meetings. For other types of meetings, a 14-day notice period is required. However, a company's articles of association may specify longer notice periods.

Members may request that directors convene a general meeting. In such an instance, the directors must respond by scheduling the meeting within 21 days.

The Companies Act permits hybrid or virtual meetings. Notices for such meetings must clearly outline how to join and participate. Additionally, companies must adhere to the provisions of their articles of association regarding the conduct of general meetings.

5.4 Shareholder Claims

The Companies Act acknowledges the concept of shareholder derivative claims, which can be made on behalf of a company. In the context of these claims, "*member*" encompasses not only those listed in the company's register of members but also individuals to whom shares have been transferred or transmitted by law. This means an applicant does not necessarily need to be officially recorded as a member or possess a share certificate. It is sufficient to demonstrate that they are beneficially entitled to the shares in question.

The grounds that the court will consider to permit a derivative claim include negligence, default, breach of duty, and breach of trust by a company director. Courts in Kenya have held that permission to commence a derivative claim will be denied where the suit is not in the interest of or of benefit to the company and where the company has authorised the proposed act.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Shareholders in publicly traded companies in Kenya are subject to various disclosure obligations, some of which are outlined below.

Notification of Holdings Above Certain Thresholds

Any person obtaining "*notifiable interest*" (ie, 3% or more) in shares of a listed company or who ceases to be interested in such shares to notify the listed company of the acquisition or cessation of interest in the shares. The Licensing Regulations also require that listed companies report to the NSE on a monthly basis:

- all persons who have acquired or cease to have a notifiable interest in its shares;
- all directors holding 1% or more in the relevant share capital; and
- cumulative holding of the relevant share capital by directors.

Disclosure Obligations for Ultimate Beneficial Owners

Subject to certain exceptions, companies incorporated in Kenya to file a register of beneficial owners. A beneficial owner is a natural person who holds at least 10% of the shares or voting rights or has the power to change directorship or significantly influence the company.

Shareholding Disclosures

Listed companies must publish detailed information about their shareholding, including:

- a quarterly disclosure to the NSE of every person who holds or acquires 3% or more of the listed company's ordinary shares;
- publication by a listed company in its annual report of:
 - (a) distribution of shareholders; and

- (b) names of the ten largest shareholders and the number of shares in which they have an interest as shown in the issuer's register of members; and
- immediate disclosure by an issuer of any information likely to have a material effect on market activity; and
- disclosure in the annual report of any substantial sale of assets involving 25% or more of the total assets.

Notification to the Kenya Revenue Authority

Every business entity is required to report to the Commissioner-General of the Kenya Revenue Authority within thirty days of any change in the ownership structure resulting in a change of ten per cent (10%) or more of the issued share capital.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Directors of a company are required to prepare annual financial statements that give an accurate and fair view of the company's financial position for the relevant year. A copy of the annual financial statement must be sent to every member of the company, every holder of the company's debentures and every person entitled to receive notice of general meetings.

In addition, directors are required to prepare a director's report for each financial year. For companies that do not qualify for exemption under the small companies regime, the report should also contain a business review containing information about the company's business.

Listed companies are required to publish their annual financial statements, as well as the director's report, on their website.

The directors are required to lodge certain documents, such as balance sheets, annual financial statements, director's reports, and auditor's reports, with the Registrar of Companies, but in practice, this is not done as the Companies Registry only provides for filing a company's annual returns.

6.2 Disclosure of Corporate Governance Arrangements

The CMA Governance Code requires institutions to explain in their annual reports how they have applied the Code's recommendations.

6.3 Companies Registry Filings

In Kenya, companies are incorporated and registered through the Business Registration Service (BRS), a statutory agency responsible for managing the incorporation process and maintaining company records. It oversees the Companies Registry, which handles regulatory filings and stores official records for all registered companies. Most services the BRS offers are now available online through the eCitizen portal.

As part of its regulatory mandate, BRS requires companies to lodge annual returns with the Registrar on the anniversary of their incorporation or, if their last return was made on a different date, on the anniversary of that date. Failure to lodge annual returns may result in the company and each officer in default being separately liable to a fine not exceeding KES200,000. The annual returns are open for inspection to the public.

Following a recent amendment of the Companies Act by the Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Act, 2023, a company may be deemed not to be carrying on business if it has failed to file annual returns or financial statements for a period of 5 years or more or where a company has failed to

lodge a copy of the register of beneficial owners after being directed to do so by the Registrar.

The Registrar of Companies has broad powers to ensure compliance with corporate obligations. These include the authority to strike off companies from the register if they appear inactive – such as those that have not submitted annual returns or financial statements for an extended period or have not provided their register of beneficial owners after being instructed to do so.

In line with these powers, BRS issued a compliance notice on 11 April 2025 to private companies that have not filed their register of beneficial owners. The notice warned that non-compliant companies may be presumed inactive or not operating, which could result in their removal from the official register of companies.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Companies are generally required to appoint an independent auditor to review their annual financial statements. There are exemptions for small and dormant companies.

Small Company

A company qualifies as “small” if its turnover for the relevant year does not exceed KES50,000,000 (approximately USD387,570) and the value of its net assets at the end of the financial year does not exceed KES20,000,000 (approximately USD155,026).

Dormant Company

A dormant company is one that has not traded or has minimal activity during the year. However, this exemption does not apply to companies in specific industries, even dormant ones. These industries include insurance companies, banking companies, and e-money issuers.

Audits

Even if a company falls under the small or dormant company exemptions, its members (owners or shareholders) can still require an audit by providing formal notice to the company.

The company’s directors or members vote to appoint and remove an auditor. A simple majority vote is required for appointment, but a special resolution from the members is required for removal.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The Companies Act and the CMA Governance Code establish specific requirements for directors in relation to risk management and internal controls.

- Directors’ report – Directors must prepare a report for each financial year. This report should include a business review detailing the company’s principal risks and uncertainties.
- Internal control systems – The boards of listed companies must:
 - (a) establish and regularly review the adequacy and integrity of the company’s internal control systems;
 - (b) ensure compliance with applicable laws and regulations; and
 - (c) establish an effective risk management framework.

Trends and Developments

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Kieti Law LLP is a leading Nairobi-based law firm specialising in corporate law and finance, operating under Cliffe Dekker Hofmeyr's umbrella. They offer a comprehensive and responsive approach, tailoring their services to meet clients' legal needs. The firm boasts a team of experienced and versatile financing lawyers with a strong reputation for exceptional service. They excel at handling complex deals and regularly advise leading Kenyan and international corporations, financial institutions, and govern-

ments on a wide range of corporate, commercial and financial matters. Leveraging its extensive experience, Kieti Law's team consistently supports companies, boards of directors, investors, and senior executives in high-stakes corporate transactions such as M&A, takeovers, and joint ventures. Their expertise also encompasses advising on corporate governance issues, including reporting requirements for listed companies, ESG best practices and shareholder rights.

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Introduction

Kenya's corporate governance landscape has undergone a profound transformation in recent years, reflecting a growing emphasis on sustainability, transparency, and accountability. A confluence of factors – including increased investor scrutiny, regulatory developments, and a heightened awareness of the social and environmental impacts of corporate activities – has driven this evolution, and the transformation has been marked by a series of legislative, regulatory, and institutional reforms that have sought to align Kenya's corporate governance framework with international best practices.

The Evolution of ESG Reporting and Integration

Regulatory drivers of ESG integration

Integrating Environmental, Social, and Governance (ESG) factors into corporate governance has become a paramount consideration in Kenya. Driven by growing investor concerns about climate change, social impacts, and ethical business practices, companies increasingly recognise the imperative of adopting sustainable strategies and reporting on their ESG performance.

Regulatory bodies have played a pivotal role in shaping the ESG landscape in Kenya. The Nairobi Securities Exchange (NSE) and the Capital Markets Authority (CMA) have issued guidelines and codes that mandate ESG disclosure and reporting for listed companies. These regulations require companies to disclose information on their governance practices, environmental and social risk management, stakeholder engagement, economic performance, anti-corruption efforts, occupational health and safety, diversity, data privacy, and emissions.

Board-Level Oversight and Sustainability Committees

A notable development in the ESG space has been the NSE's encouragement of listed companies to establish dedicated sustainability committees at the board level. These committees oversee the implementation of ESG strategies and ensure sustainability is embedded in corporate decision-making. The formation of such committees signals a shift from ESG being a peripheral concern to becoming a central pillar of corporate governance.

The CMA's Code of Corporate Governance Practices for Issuers of Securities to the Public

has also been updated to reinforce the importance of board diversity, stakeholder engagement, and the protection of minority shareholder rights. These changes reflect a broader recognition that effective ESG governance is integral to long-term corporate success and resilience.

Sector-Specific ESG Guidelines and Initiatives

In Kenya, guidelines tailored to the ESG sector have emerged across various industries, promoting the adoption of sustainable practices. These guidelines offer specific recommendations to companies in areas such as banking, energy, and agriculture, enabling them to effectively address the unique ESG challenges and opportunities specific to their industries.

For example, the Kenya Bankers Association (KBA) has adopted the Sustainable Finance Initiative (SFI) industry principles for the banking sector. The SFI requires banks to establish environmental and social risk management systems, monitor clients' associated risks, and ensure compliance with labour standards. To promote sustainable finance practices, the KBA has also introduced an e-learning platform and the SFI Catalyst Awards, which incentivise best practices and recognise leadership in sustainable finance.

The Central Bank of Kenya (CBK) has issued the Guidance on Climate-Related Risk Management, which outlines recommendations for banks to manage climate-related financial risks. The main recommendations contained in the CBK Guidance include:

- the board of directors is responsible for overseeing the institution's exposure to and responses to climate-related issues;

- the board of directors is tasked with formulating and implementing strategies and policies to manage climate-related financial risks;
- institutions are required to integrate climate-related risk considerations into their risk management frameworks;
- institutions should develop systems for reporting on the management of climate-related risks; and
- institutions in the banking sector are required to submit a time-bound plan approved by the institution's board on implementation of the Guidance and, in addition, a quarterly report on the progress of implementation of this plan within 10 days after the end of every calendar quarter from the quarter ending 30 September 2022.

The CBK has also published the draft Kenya Green Finance Taxonomy, providing a standardised framework for green finance and facilitating informed decision-making on environmentally friendly investments. It outlines a minimum set of assets, projects, and activities that qualify as "green" according to international best practices and national priorities. Through the Green Finance Taxonomy, banks will be able to make informed decisions on environmentally friendly investments that will help to promote sustainable development.

Legislative Developments: The Climate Change Act and Private Sector Obligations

Under the Climate Change Act, Chapter 387A of the Laws of Kenya, the Climate Change Council and the Cabinet Secretary responsible for climate change can impose obligations on private entities, such as companies. These obligations require the entities to implement actions that align with the national goal of achieving low-carbon, climate-resilient development. If a private entity is given such an obligation, it must

prepare reports detailing its performance regarding these climate change responsibilities, as well as the actions it has taken, is currently taking, or plans to take to meet these responsibilities in the future.

The Impact of ESG on Corporate Strategy and Investment

The growing emphasis on ESG has profoundly impacted corporate strategy and investment in Kenya. Companies increasingly recognise that strong ESG performance can enhance their reputation, attract investment, and mitigate risks associated with environmental and social issues. Domestic and international investors are placing greater weight on ESG factors in their investment decisions, leading to increased demand for transparent and comprehensive ESG reporting. This trend is expected to continue, with ESG considerations becoming integral to Kenya's corporate governance and risk management.

Strengthening Anti-Money Laundering and Beneficial Ownership Regimes

Legislative reforms: The Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Bill, 2025

The prevention of money laundering and terrorist financing has been a key priority for the Kenyan government. To combat these illicit activities, the government has implemented robust anti-money laundering (AML) legislation that requires companies to enhance transparency and disclosure. The National Assembly recently passed the Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Bill, 2025, to strengthen Kenya's anti-money laundering and terrorism financing regulatory framework. Once enacted, the Bill will amend ten Acts of Parliament and expand the scope of Anti-Money Laundering and Combating of Terrorism oversight to traditionally non-financial sectors, such

as real estate, legal, and accounting services, which have historically been vulnerable to illicit financial flows.

Beneficial ownership disclosure requirements

One of the most significant AML measures is the Companies (Beneficial Ownership Information) Regulations, which mandate companies to disclose their beneficial owners. This disclosure requirement helps to prevent the misuse of corporate structures for illicit activities and enhances transparency in corporate ownership.

Beneficial owners are individuals who ultimately control or benefit from a company, regardless of their direct ownership stake, and include a natural person who meets any of the following conditions:

- holds at least 10% of the issued shares in the company either directly or indirectly;
- exercises at least 10% of the voting rights in the company either directly or indirectly;
- holds a right, directly or indirectly, to appoint or remove a director of the company; or
- exercises significant influence or control, directly or indirectly, over the company.

Amendments to the Companies Act and the Limited Liability Partnership Act have further strengthened anti-money laundering measures by extending disclosure requirements to include nominee shareholders and partners, respectively. Nominee shareholders hold shares on behalf of others, while nominee partners act as partners in a limited liability partnership on behalf of others. By requiring disclosure of these individuals, the government aims to prevent the use of nominees to conceal the true beneficial owners of companies and facilitate illicit activities.

Enhanced enforcement and compliance mechanisms

The Registrar of Companies has intensified compliance audits and imposed penalties for non-disclosure of beneficial ownership information. The threshold for beneficial ownership disclosure remains at 10% of issued shares or voting rights, but recent amendments have closed loopholes by requiring the disclosure of nominee shareholders and partners.

The Banking Act has been amended to include beneficial ownership in defining “*significant shareholders*.” This change means that the CBK must vet individuals identified as beneficial owners before they can be appointed as significant shareholders in banking institutions. The requirement is intended to ensure that only individuals with clean records and no connections to illicit activities are involved in the ownership and management of banks.

International Alignment and Cross-Border Cooperation

Kenya’s efforts to strengthen its AML and beneficial ownership regimes are aligned with international standards, including those set by the Financial Action Task Force (FATF). The country has also enhanced cross-border cooperation with other jurisdictions to combat money laundering and terrorist financing, recognising the global nature of these threats. These measures have improved Kenya’s reputation as a safe and transparent destination for investment and business.

Formalisation of the Role of Company Secretaries and Contact Persons

Regulatory changes and the expanding role of company secretaries

The role of company secretaries has become increasingly important in the Kenyan corpo-

rate governance landscape. Traditionally, the appointment of company secretaries was not mandatory for all companies. However, recent regulatory changes have made it more common for companies, particularly private companies and companies limited by guarantee, to appoint company secretaries or contact persons.

Private companies or companies limited by guarantee that lack a company secretary or resident director must appoint a contact person. The Companies Act mandates this role and requires the contact person to maintain critical company records, including those related to directorships, shareholding, beneficial ownership, and any other information required by law. Notably, the contact person must be a natural person with a permanent Kenyan residence.

Enhancing Local Accountability and Regulatory Oversight

The formalisation of the role of company secretaries and contact persons is intended to enhance local accountability and facilitate regulatory oversight. By ensuring a designated individual is responsible for maintaining statutory records and compliance with legal requirements, regulators can more effectively monitor and enforce corporate governance standards.

This development is particularly significant for private companies and companies limited by guarantee, which may not have previously been subject to the same level of scrutiny as public companies.

Professionalisation and capacity building

The evolving role of company secretaries has also led to increased professionalisation and capacity building within the profession. Company secretaries are now expected to possess a deep understanding of corporate governance

principles, legal and regulatory requirements, and best practices in risk management and compliance. Professional bodies and training institutions have responded by offering specialised courses and certifications to equip company secretaries with the skills and knowledge needed to fulfil their expanded responsibilities.

Technological Advancements and Digital Compliance

Digitalisation of corporate governance processes

A significant recent trend is the adoption of technology to streamline corporate governance compliance. The Office of the Registrar of Companies has digitised the submission of beneficial ownership information and other statutory filings, improving transparency and efficiency. This digital transformation has facilitated real-time compliance monitoring and made it easier for regulators to identify and address non-compliance. Companies can now submit required information electronically, reducing administrative burdens and minimising the risk of errors or omissions.

Enhancing transparency and accessibility

The digitisation of corporate governance processes has also enhanced transparency and accessibility. Stakeholders, including investors, regulators, and the public, can more easily access information about companies, their ownership structures, and compliance status. This increased transparency helps to build trust in the corporate sector and supports informed decision-making by investors and other stakeholders.

Leveraging technology for risk management and reporting

Beyond compliance, companies increasingly leverage technology to enhance risk management

and reporting. Advanced data analytics, artificial intelligence, and blockchain technologies are being explored to improve the accuracy and reliability of corporate governance data, detect potential risks, and ensure timely and accurate reporting. These technological advancements are expected to play an increasingly important role in shaping Kenya's corporate governance future.

Ongoing Challenges and Opportunities for Reform

Awareness and understanding of corporate governance principles

Despite the significant progress made in corporate governance in Kenya, several challenges remain. One key challenge is the lack of awareness and understanding of corporate governance principles among some stakeholders, particularly in smaller companies. Many SMEs may not fully appreciate the importance of robust corporate governance or may lack the resources and expertise to implement best practices. This gap underscores the need for targeted training and education programmes to build capacity and promote a culture of good governance across the corporate sector.

Enforcement and Compliance

While enforcement of corporate governance regulations has improved, resource and capacity constraints continue to pose challenges. Regulatory bodies may face difficulties monitoring compliance across a large and diverse corporate sector. Continued strengthening of enforcement mechanisms and establishing independent oversight bodies can help improve compliance and accountability. There is also a need for greater coordination and collaboration among regulatory agencies to ensure a consistent and effective approach to corporate governance.

Balancing Regulation and Innovation

As Kenya's corporate governance framework continues evolving, policymakers must balance regulation and innovation. Overly prescriptive regulations may stifle innovation and entrepreneurship, while insufficient regulation can undermine investor confidence and expose the corporate sector to risks. Ongoing dialogue between regulators, industry stakeholders, and the broader public is essential to ensure that the regulatory framework remains fit for purpose and supports sustainable economic growth.

Opportunities for Technological Innovation

The adoption of technology presents significant opportunities for enhancing Kenya's corporate governance. Digital platforms can streamline compliance processes, improve transparency, and facilitate real-time monitoring and reporting. Emerging technologies such as blockchain and artificial intelligence have the potential to revolutionise corporate governance by providing secure, tamper-proof records and enabling predictive analytics for risk management. Policymakers and industry leaders should continue to explore and invest in technological solutions to address existing challenges and drive continuous improvement in corporate governance.

The Role of International Standards and Best Practices

Alignment with global norms

Kenya's corporate governance reforms have been informed by international standards and best practices, including those set by the Organisation for Economic Cooperation and Development (OECD), the International Finance Corporation (IFC), and the Financial Action Task Force (FATF). By aligning its legal and regulatory framework with global norms, Kenya has enhanced its attractiveness as a destination for investment and business. This alignment also

facilitates cross-border cooperation and supports the integration of Kenya's corporate sector into the global economy.

Participation in Regional and International Initiatives

Kenya has actively participated in regional and international initiatives to promote good corporate governance, combat money laundering, and foster sustainable development. These initiatives provide opportunities for knowledge sharing, capacity building, and adopting best practices. Continued engagement with international partners will be essential to sustaining progress and addressing emerging challenges in corporate governance.

Conclusion

We have witnessed a consolidation and expansion of Kenya's corporate governance framework. The intensification of ESG reporting requirements, the strengthening of anti-money laundering and beneficial ownership disclosure regimes, the formalisation of the company secretary's role, and the adoption of digital compliance tools all signal a robust and evolving governance environment.

These developments align Kenya with international best practices and position its corporate sector to attract investment, foster sustainable growth, and contribute to national development. Continued focus on education, enforcement, and technological innovation will be essential to sustaining this positive trajectory and addressing the remaining challenges in corporate governance.

As Kenya continues on its path of reform, the lessons learned and best practices adopted will serve as a model for other emerging markets seeking to enhance their corporate governance frameworks and achieve sustainable economic development.

LIECHTENSTEIN

Law and Practice

Contributed by:

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Schurti Partners Attorneys-at-Law Ltd. is a Liechtenstein-based full-service law firm with a strong focus on cross-border matters. The firm's lawyers were trained and are qualified in several jurisdictions (Austria, California, England and Wales, Germany, Ireland, Liechtenstein, New York and Switzerland), and have gained work experience abroad in some of the most prestigious international law firms. The firm was founded in 1991 as a partnership and incorporated in 2015. Over the years, it has grown to become one of the largest and most renowned

law firms in Liechtenstein. Schurti Partners has established a solid track record of supporting clients with businesses and/or assets across the world, drawing on the support of the firm's well-established networks of leading independent law firms based in other jurisdictions. Today, it is one of the leading Liechtenstein law firms in the area of corporate and commercial law and M&A transactions and regularly handles complex matters in these areas for large corporate clients and regulated financial service providers in these areas.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The predominant form is the corporation (*Aktiengesellschaft*). For smaller business entities the Liechtenstein establishment (*Anstalt*) is also quite common; however, it is less popular in an international context. The limited company (*Gesellschaft mit beschränkter Haftung*) plays a less significant role in practice. Likewise, the European Company (*Societas Europaea*/SE) is not very common in Liechtenstein.

1.2 Sources of Corporate Governance Requirements

There is no separate piece of legislation or special code for corporate governance rules in Liechtenstein. Therefore, the key legislative source is the Liechtenstein Persons and Companies Act (PCA), which is not only the fundamental piece of legislation for Liechtenstein companies of any type, but also provides the legal framework for Liechtenstein corporations.

Due to Liechtenstein's EEA membership, the SE EU Council Regulation (EC) 2157/2001 of 8 October 2001 applies directly in Liechtenstein. As a result, Liechtenstein enacted its national SE Act, which complements the aforementioned EU Regulation.

At present, Liechtenstein does not have a stock exchange of its own. However, recently the Liechtenstein legislature enacted a Trading Place and Exchange Act (TPEA) which entered into force on 1 February 2025. The TPEA lists rules and provisions of best practice for listed companies. Furthermore, the TPEA includes the regulatory framework for the operation of stock exchanges and other trading venues in Liechtenstein. It remains to be seen to what extent

the TPEA will become relevant in practice. To date, and in the absence of a Liechtenstein stock exchange, only a small number of Liechtenstein companies have been listed on foreign stock exchanges in Switzerland or in EEA member states.

Furthermore, there are a number of laws that deal with similar rules, such as the Takeover Act (*Übernahmegesetz*) and the Disclosure Act (*Offenlegungsgesetz*). In addition, such Liechtenstein companies are subject to certain Liechtenstein law requirements (Article 1096a PCA), one of which constitutes the obligation to prepare a corporate governance report.

In addition, for supervised corporations, such as banks, life insurers or asset managers, additional laws that form part of the financial services regulation are relevant, such as the Banking Act, the Insurance Supervision Act and the FMA Act.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

As only very few Liechtenstein companies have issued shares which are publicly traded, there is no comprehensive specific corporate governance legislation in separate laws or rules.

The PCA also includes a few mandatory corporate governance requirements. In particular an undertaking of public interest must have a separate committee of its supreme executive body (*Prüfungsausschuss*). It is the task of this committee to review and supervise the internal accounting, control and risk management systems as well as the sustainability reporting and to report to the supreme executive body of the company about its findings.

Furthermore, Liechtenstein companies which have issued shares that are publicly traded in another EEA member state must issue a corporate governance report as part of their annual report. This corporate governance report must include, inter alia, all relevant information on the corporate governance policies and practices (including any specific corporate governance code) that the company is subject to.

Under the TPEA, there are noteworthy corporate governance requirements for stock exchange operator companies.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

It is expected that Liechtenstein will implement EU Directive 2019/2121 on cross-border conversions, mergers and spin-offs before the end of 2025. The resulting new provisions in the PCA will provide Liechtenstein corporations and their shareholders and board members with additional options for domestic and cross-border M&A transactions, which may contribute to the more effective implementation of corporate governance systems.

Furthermore, hot topics include environmental, social and governance (ESG) issues, corporate social responsibility (CSR) and the implementation and adaptation of the sanction regime triggered by the conflict between Russia and Ukraine.

Comprehensive amendments to the PCA have been enacted to implement Directive (EU) 2019/1151. These new rules permit the possibility of digitally incorporating certain companies. Furthermore, certain digital notarisation and cer-

tification services have been introduced since 1 May 2025.

The cross-border exchange of information via the European System of Register Interconnection is intended to be expanded.

After the COVID-19 pandemic, the Liechtenstein legislature decided to maintain certain transitional provisions aimed at facilitating the holding of shareholder and board meetings. Consequently, the PCA was amended to permit virtual board and shareholder meetings and to provide enhanced legal certainty for hybrid shareholder and board meetings.

2.2 ESG Considerations

Due to Liechtenstein's EEA membership, ESG issues have become very relevant for Liechtenstein companies in relation to reporting. Liechtenstein continuously implements pertinent EEA/EU directives dealing with ESG matters. Therefore, it is not a surprise that recent legislative changes to the PCA provide for various obligations in this regard. Article 1096b PCA lists the factors that a Liechtenstein company must comply with in relation to reporting and auditing. The specific obligations of a Liechtenstein company depend on such company's size. It is fair to conclude that ESG-related matters nowadays constitute important elements in the corporate governance system of Liechtenstein companies. Public companies must also report on sustainability matters in their annual corporate governance report.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The fundamental structure of a Liechtenstein corporation (AG) is not very complex. The vast majority of Liechtenstein corporations have a one-tier system which provides for a board of directors. The supreme executive/management body of a Liechtenstein corporation is the board of directors. Additional supervisory bodies are not common in Liechtenstein, but are permissible under statutory law.

It is possible for the board of directors to directly manage the corporation. Alternatively, as it is the case in larger corporations, the board of directors can delegate operations and daily management to the executive management (*Geschäftsleitung*). Liechtenstein law allows such delegation to be very comprehensive. However, the general supervision duty and the ultimate responsibility to keep the corporation in a financially sound condition must not be delegated. A delegation to the executive management must be dealt with in separate organisational regulations (*Organisationsreglement*). It is also possible that such regulations permit “*personal overlaps*” so that a board member can also be a member of the executive management. The organisational regulations must define the powers which remain with the board of directors and the powers that are delegated to the executive management body.

Liechtenstein law does not require board members to comply with any statutory independence requirements. Nonetheless, case law has adopted, in some decisions, the principle that in order to avoid or mitigate personal liability, a board member must have sufficient availability,

capacity, and time to duly and carefully fulfil its obligations as a board member in a corporation.

Employees are not entitled to send representatives to sit on the board of directors of a Liechtenstein corporation. Nonetheless, it is possible that the articles of a corporation provide that a member of the employees is entitled to a seat on the board.

3.2 Decisions Made by Particular Bodies

Under statutory law the board of directors is obligated to prepare any business for the general meeting of shareholders and to carry out the resolutions to set up any regulations which are necessary for an orderly business activity, to supervise the persons trusted with the management and the representation of the company and to supervise the implementation of any legal requirements, articles and internal regulations, to advise regularly on the management of the business and take any necessary measures, and, where applicable, inform the court in the event of any approaching insolvency of the company.

A supervisory board (*Aufsichtsrat*) is optional under Liechtenstein law. If installed, the task of this board is to supervise the management and the administration of the company.

The board of directors and, where applicable, the supervisory board, can opt to install one or more committees with specific tasks.

Furthermore, the general meeting of shareholders is the supreme body of a corporation. Its tasks under statutory law are the election of the board of directors, the appointment of the auditors, the approval of the annual accounts and the assessment of the results and dividends, the discharge of the board of directors, the passing of resolutions regarding any amendment of the

articles and the passing of resolutions on matters which are reserved to the general meeting by law or by the articles of the company.

3.3 Decision-Making Processes

The shareholders' meeting, as the supreme body of a Liechtenstein corporation, passes its resolutions by way of ordinary or extraordinary meetings. Typically, the articles of association and the PCA spell out the specific rules for the convocation and the holding of such meetings (see 5.3 Shareholder Meetings).

Conversely, Liechtenstein statutory law provides for only a very limited number of general rules in relation to the meetings and resolutions of the board of directors and the executive management body. Additional statutory provisions exist for companies that are under the supervision of the Liechtenstein financial market authority (FMA). However, the corporation's articles of association or internal specific relations can include detailed provisions in this regard.

4. Directors and Officers

4.1 Board Structure

Please see 3.1 **Bodies or Functions Involved in Governance and Management**. The board of directors of a corporation that does not have/does not require any Liechtenstein licence must include at least one member who possesses the qualification or licence to act as a professional trustee (see 4.4 **Appointment and Removal of Directors/Officers**).

4.2 Roles of Board Members

Typically, a board of directors consists of a chairman/president and other board members. The chairman is usually in charge of organising the board meetings. In many boards there is also

usually a vice president/vice chairman who steps in when the chairman is absent. The other members can also be allocated specific tasks. In large boards there can also be internal committees provided that the articles of association permit this.

Although not mandatory, it is a common task of the chairman of the board of directors to also preside over the shareholder meetings of the company. Frequently, the corporation's articles of association allocate additional roles to the chairman, the vice chairman and/or the other board members.

4.3 Board Composition Requirements/Recommendations

Please see 4.2 **Roles of Board Members**.

4.4 Appointment and Removal of Directors/Officers

Basically, it is the task of the general meeting of shareholders to elect and re-elect the members and the chairman of the board of directors. To the extent not dealt with differently in the corporation's articles, a simple majority of the votes is required for such election.

As far as the removal of members of the board of directors and the executive management is concerned, corporate decisions to remove such members are the exception rather than the rule. It is more common for a member to resign unilaterally or not to stand for re-election.

In the vast majority of cases, the board of directors appoints the members of the executive management body. However, there are corporations that also require a shareholder vote for the appointment of such members.

Under Liechtenstein law, there is no general obligation for the board of directors to consist of more than one member. However, for corporations with a nominal share capital exceeding the amount of CHF1 million, the board of directors must consist of at least three members. Board members can either be individuals or legal entities/corporate directors. For certain regulated companies (such as banks, insurers or asset managers), specific requirements apply pursuant to the pertinent legislation.

It should be noted that the board of directors is free to organise itself within the ambit of statutory law. Consequently, the board of directors can also set up internal committees for specific purposes in order to enhance the corporate governance and organisation of the corporation.

For corporations that are not subject to any licence requirement to carry out its activities, the law requires that at least one board member must be a citizen of Switzerland or an EEA state and in possession of a licence as a professional trustee, or a licence pursuant to Article 180a PCA.

4.5 Rules/Requirements Concerning Independence of Directors

In general, members of the board of directors are not under a statutory law requirement to be independent from any shareholder of the respective corporation. Nonetheless, the PCA contains specific rules regarding independence requirements within the specific audit committee (*Prüfungsausschuss*): in a nutshell, these rules require that the majority of the members of this committee must be independent of the respective corporation (including the chairman of this committee).

General company rules in the PCR further include mandatory requirements regarding the voting rights on matters or business transactions between the company and him-/herself or a person close to him/her if such transaction results in a personal advantage for such board member. Furthermore, board members may not or must not participate in any shareholder vote on their discharge.

4.6 Legal Duties of Directors/Officers

Under Liechtenstein law, board members must act in accordance with the principles of the business judgement rule. When doing so, they must safeguard the best interests of the corporation and act on the basis of adequate information, without bias and free of any conflict of interests. When doing so, they must also consider the interests of the employees and other stakeholders. The general legal duties of the board members include their statutory duty of care and loyalty to the corporation. Furthermore, the members of the board must treat the shareholders of the corporation equally in the same circumstances.

The above rules apply accordingly to members of the executive management body.

4.7 Responsibility/Accountability of Directors

Under Liechtenstein law, the board of directors is responsible for ensuring sufficient corporate governance. However, statutory law does not include explicit provisions that would constitute a specific legal obligation for the board in this regard. The law, however, contains various single tasks that must be duly organised and complied with by the board of directors. Such tasks include the overall management, financial situation, and organisation of the corporation, as well as the supervision of the members of the management body. The board must also ensure

that the corporation's financial documents are in line with the applicable accounting standards.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Depending on the claim at hand, the corporation itself or, alternatively, the creditors of the corporation can enforce such a breach. If such breach can be proven, the main consequence for the respective board member will be an obligation to pay damages. For board members of regulated companies, additional sanctions may apply. To the extent the breach also qualifies as a crime under the Liechtenstein Criminal Code, the sanctions can also include fines and imprisonment.

Liechtenstein law provides for the personal liability of board members in the event they have infringed their legal obligations and duties. For such liability, not only damage must be proven, but also that the board member acted intentionally or negligently, and that such conduct caused the damage. The liability of various board members is of joint and several nature. Board members are liable for their wilful or intentional misconduct and their negligence. If a board member is liable for damages, the legal entity can only assert such damages against a board member if such board member has not been released from liability due to a discharge resolved by the shareholder meeting. If the corporation has no claim for damages, it is possible that the shareholders can directly enforce their claim for damages against the board members.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

It is common for board members and/or the members of the management of larger corporations to be insured under a D&O insurance. In this context, it is acceptable that the respective

company pays the insurance premium for the board members and the members of the management.

However, it would not be compatible with the law if the company accepted an obligation to indemnify the board members, and the members of the management against any and all liabilities that they incur towards the company or its shareholders. Nonetheless, it is possible for a company to agree to such indemnity in a specific case/lawsuit.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

This depends on the size of the company. For smaller companies there are no major statutory law restrictions, but market practice will frequently set the limits for the respective remuneration/fee amounts. Conversely, for public companies a number of statutory law restrictions exist under the PCA and under certain regulatory laws. The latter, however, apply only to the respective regulated companies, such as banks or insurers. For listed companies, shareholder approval may be required for the remuneration of board members and members of the management.

4.11 Disclosure of Payments to Directors/Officers

Publicly traded companies must disclose this information in their annual report. For regulated companies, such as banks and insurers, additional specific requirements exist in this regard (also regarding the structure and the degree of detail for such disclosure).

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Under Liechtenstein law, shareholders do not owe any duty of care, loyalty, or any other duty to the corporation. This principle applies to both minority and majority shareholders in their capacity as shareholders.

Conversely, shareholders, in proportion to their voting powers, can influence the key decisions to be taken in relation to corporate governance issues at the level of the shareholder meeting. In this regard, their voting rights can prove a useful tool to supervise and influence the board of directors and its strategy. However, under Liechtenstein law, a shareholder is neither required to participate in the shareholder meeting, nor to exercise his/her voting right on any agenda item of such meeting.

Depending on the scope of their participation, shareholders are subject to certain statutory disclosure requirements as regards their shareholdings. Such obligations apply to shareholders of listed corporations, or companies that are regulated by and under the supervision of the Liechtenstein FMA.

5.2 Role of Shareholders in Company Management

Liechtenstein law does not impose on the shareholders of a Liechtenstein company any duty or obligation except for the obligation to pay up the shares that they subscribed. In particular, the shareholders do not owe the company a duty of care or loyalty. It should be noted that, under Liechtenstein law, a shareholder cannot be forced to exercise his/her voting rights.

However, if a shareholder is also a member of the board of directors, he/she will be subject to the duties owed by board members to the corporation, in particular, a duty of care and loyalty.

5.3 Shareholder Meetings

Unless a company's articles require a larger number of meetings, there shall be at least one shareholder meeting per year (annual shareholder meeting/ordinary shareholder meeting). At the occasion of such annual general meeting, the key decisions are taken by the shareholders on financial matters (annual accounts, use of profits, other financial aspects for which a shareholder vote can be required under a corporation's articles, etc). In addition, the shareholders at such meeting decide on the discharge of the board of directors and, in some instances, of the management board and, to the extent necessary, elect or re-elect members of the board of directors and the auditor of the corporation.

If all shareholders are present or validly represented by a proxy, the shareholder meeting qualifies as "*universal/full shareholder meeting*" for which the requirements and timelines regarding the calling of a shareholder meeting do not apply. Shareholders who jointly hold 10% of all countable votes arising from the share capital are entitled to request the calling of a shareholder meeting. In addition, shareholders of at least 5% of all the votes arising from the corporation's share capital are entitled to request that an item be placed on the shareholder meeting agenda.

Furthermore, it is possible to hold additional/extraordinary general shareholder meetings. Such meetings can be convened by the board of directors in accordance with the articles and statutory law. It is also permissible for a shareholder who represents at least 10% of the corporation's share capital to request the board to

convene such extraordinary shareholder meeting. For publicly traded companies, this threshold is lower.

It is now possible to hold virtual shareholder meetings provided that the articles of a corporation permit the holding of such virtual meetings.

It should be noted that, for certain material shareholder resolutions, simple majorities are not sufficient. For such resolutions, a qualified majority (as defined in the articles or by statutory law) will be required. This can de facto result in a blocking power of majority shareholders, the consent of whom would be required to reach a qualified majority.

5.4 Shareholder Claims

For instance, a shareholder can be entitled to sue a member of the board of directors or the corporation's auditor on the shareholder's own behalf or, in a scenario of the corporation's financial distress, on behalf of the corporation – eg, for breach of duties (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**).

Furthermore, a shareholder can challenge a shareholder resolution, provided that such legal action complies with the statutory requirements and (relatively short) timelines.

However, a shareholder cannot challenge a decision of the board of directors or of the management body. Nonetheless, the law grants protection since board resolutions that infringe basic rules qualify as null and void. A shareholder can therefore submit such resolution to the court and request that the court declare such resolution null and void.

5.5 Disclosure by Shareholders in Publicly Traded Companies

There are no such limitations as far as the maximum number or percentage of shares or securities held by a shareholder is concerned. However, it is possible that a corporation's articles include such limit, as far as the exercise of voting rights is concerned (also by introducing different share categories with different voting rights).

Conversely, Liechtenstein laws provide for certain disclosure obligations. Such obligations mainly concern listed companies and other companies that are regulated by and supervised by the Liechtenstein FMA. If an investor acquires or sells, directly or indirectly, shares in such company so that his/her voting rights reach, depending on the type of target, exceed or fall below 5%, 10%, 15%, 20%, 25%, 33%, 50% or 66%, such transaction and the resulting new shareholdings must be notified in advance to the FMA and to the target company. The Disclosure Act (*Offenlegungsgesetz*) further provides very detailed disclosure rules for a number of different scenarios. However, these rules only apply to Liechtenstein corporations that are listed on a stock exchange.

In accordance with anti-money laundering legislation, a corporation must register, on a timely basis, those of its shareholders/beneficial owners that hold more than 25% of the voting rights/share capital (or do otherwise control the corporation) in the Register of Beneficial Owners, which is maintained by the Office of Justice in Vaduz.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

The ultimate responsibility for disclosure and transparency lies with the board of directors. In particular, the board is responsible for drawing up the annual report. The auditors must review this annual report.

Liechtenstein law does not impose a general obligation on a Liechtenstein corporation to disclose its corporate governance or to report thereon. However, Liechtenstein corporations that have issued securities listed on the regulator market in the EEA must include and publish a specific corporate governance report in their annual report. Article 1096a PCA lists in detail the required content for such corporate governance report.

Pursuant to Article 182a PCA, the members of the board of directors of a legal entity have a collective duty to ensure that the required accounting documents, as well as the corporate governance report, are prepared and disclosed in accordance with the provisions on accounting.

Furthermore, institutional investors and asset managers shall develop and publicly disclose a participation policy. The participation policy shall describe how institutional investors and asset managers monitor the companies in which they have invested with regard to important matters, in particular with regard to corporate governance. Liechtenstein companies that are subject to foreign listing rules, due to their listing on a foreign stock exchange, are subject to such foreign listing rules.

6.2 Disclosure of Corporate Governance Arrangements

Please see 1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares.

6.3 Companies Registry Filings

The Office of Justice (*Amt für Justiz*) in Vaduz maintains the commercial register in Liechtenstein. Liechtenstein corporations must be registered in this commercial register in order to come into legal existence. Furthermore, any subsequent changes of the articles of association of such corporation must be registered as well. Additional filings which a Liechtenstein corporation is obligated to submit to the Office of Justice include the appointment (and any subsequent changes) of the persons who can represent that corporation, their signing powers, the annual accounts and any change in such company's structure, such as a liquidation, merger or spin-off.

The consequences of failing to make such filings include the nullity of the respective appointments and changes towards third parties. The Office of Justice has supervisory powers in relation to the due organisation of a Liechtenstein corporation. Therefore, it can intervene and request a corporation to rectify any non-compliance with the minimal standards set forth by Liechtenstein statutory law – eg, a sufficient number of board members or representatives.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

A Liechtenstein corporation must have an external auditor that meets the statutory requirements of independence. Such an auditor is an external organ/body of the corporation. For smaller cor-

porations/companies, it is possible to opt out of the auditor requirement.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The board of directors is responsible for drawing up the annual accounts/report of the corporation, which must then be reviewed by the auditors.

MALAYSIA

Law and Practice

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David Lai & Tan is a reputable and dynamic law firm established in 2013 by Dato' Tan Yee Boon, Mr David Lai Chung Yew and Mr David Cheong. Based in Kuala Lumpur, Malaysia, the firm offers a full spectrum of legal services, focusing on both contentious and non-contentious corporate and commercial matters. With a dedicated team of experienced advocates and solicitors, David Lai & Tan serves a diverse clientele including public-listed companies, investment banks and multinational corporations. The firm is highly regarded for its practical, high-quality

and solution-oriented legal advice. David Lai & Tan has been consistently recognised by leading law directories, including Chambers Asia Pacific (2024–25) for corporate/commercial: equity capital markets. Key areas of expertise include initial public offerings (IPOs), mergers and acquisitions (M&As), corporate restructuring and shareholder disputes. Known for its partner-led approach and unwavering professionalism, the firm continues to uphold the highest standards of legal practice.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

In Malaysia, there are seven primary forms of corporate or business organisations, each with distinct legal and regulatory requirements, as well as advantages and limitations. These forms include:

- sole proprietorship;
- general partnership;
- limited liability partnership (LLP);
- private limited company (also known as *Sendirian Berhad* or Sdn Bhd);
- public limited company (also known as *Berhad* or Bhd);
- company limited by guarantee; and
- foreign company.

The choice of structure depends on various factors, including the nature of the business, its size, the objectives of the business and the preferences of the owners.

1.2 Sources of Corporate Governance Requirements

In Malaysia, the Companies Act 2016 (“CA 2016”) serves as the principal legislation governing the management and operation of companies. It outlines essential provisions regarding the roles and responsibilities of directors, shareholders’ rights and the operational procedures for corporate decision-making. CA 2016 applies to all companies registered in Malaysia, ensuring proper management and accountability.

Beyond CA 2016, corporate governance in Malaysia is also shaped by a robust framework of regulatory and voluntary guidelines. For public listed companies, the listing requirements set by Bursa Malaysia Securities Berhad (“*Bursa Malay-*

sia”) (the “*Listing Requirements*”) are an essential source of corporate governance. These requirements cover areas such as corporate reporting, the composition of the board of directors (the “*Board*”) and the necessary approvals for major corporate decisions. Adherence to these rules is crucial for maintaining market integrity and protecting investors.

Additionally, the Malaysian Code on Corporate Governance (MCCG), introduced by the Securities Commission Malaysia (SC), offers a set of guidelines that promote transparency, integrity and strong governance practices within companies. While not mandatory, listed companies are expected to comply with the code or provide a rationale for any deviations.

Finally, companies must also reference various guidelines and circulars issued by regulatory bodies such as the Companies Commission of Malaysia (CCM), Bursa Malaysia and the SC. These documents provide updates and detailed instructions, ensuring that companies align with evolving governance standards. Such dynamic governance mechanisms are particularly vital in an era of heightened investor scrutiny, environmental expectations and global business complexity.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Corporate Governance for Publicly Traded Companies

Public listed companies in Malaysia are traded on Bursa Malaysia, which operates three distinct markets: the main market, the ACE market and the LEAP market. The main market is designed for established, large-scale companies, the ACE market targets fast-growing companies and the LEAP market focuses on smaller, emerging

businesses, providing them with opportunities for fundraising and greater market exposure. All companies in these markets are required to adhere to specific corporate governance standards.

Regulatory Framework for Corporate Governance

These companies must comply with several key regulations that govern corporate governance. CA 2016 provides the legal foundation, detailing the roles of directors and the rights of shareholders. The Listing Requirements impose mandatory governance obligations on listed companies, such as the composition of the Board, financial disclosures and the establishment of essential committees like audit and risk management. These requirements ensure that companies maintain a high level of transparency and accountability.

Moreover, these regulatory requirements support Malaysia's broader goals of enhancing investor protection, promoting ethical corporate behaviour and attracting foreign investment through strong governance practices.

In addition, the MCGG offers guidelines for best practices in corporate governance. While adherence to the MCGG is not compulsory, listed companies are expected to either follow its principles or explain any deviations. This flexible approach allows companies to maintain governance standards while providing transparency regarding their corporate practices.

The MCGG's emphasis on board diversity, stakeholder engagement and sustainability aligns with global trends and reinforces Malaysia's commitment to responsible business conduct.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

As Malaysia looks towards 2025, corporate governance continues to evolve in response to global trends, regulatory developments and heightened stakeholder expectations. The following key issues are poised to take centre stage in the governance landscape.

Environment, Social and Governance (ESG) Compliance

ESG factors are becoming increasingly important in corporate governance. The Malaysian government and regulators, particularly the SC and Bursa Malaysia, are expected to implement more structured frameworks for ESG disclosures and practices among public listed companies. Companies will be expected to provide clear and measurable outcomes related to environmental impact, social responsibility and governance practices. This growing focus on ESG is aligned with global trends and reflects an increasing demand from investors for transparency in these areas.

This focus on ESG aligns with global investor demands and Malaysia's commitment to sustainable development. Increasingly, investors are prioritising companies with credible ESG credentials, making ESG integration not only a compliance matter but also a competitive differentiator.

Board Diversity and Inclusion

Diversity in the boardroom is another hot topic that will continue to gain traction in 2025. Improving gender diversity and inclusion at the leadership level is becoming more of a priority for regulators and investors alike. Bursa Malaysia and the SC are likely to enhance regulations aimed at increasing diversity, ensuring that the

Board is not only more inclusive but also better positioned to navigate the complexities of modern business environments.

Digital Governance and Cybersecurity

With Malaysia's ongoing digital transformation, digital governance and cybersecurity are becoming increasingly critical. The increase in digital transformations and the rising frequency of cyber threats mean that companies will need to establish robust cybersecurity frameworks and governance structures to protect sensitive data. Regulators are likely to introduce more stringent disclosure requirements on cybersecurity readiness, especially for companies handling sensitive consumer or financial data. Directors are also expected to develop digital literacy and be accountable for overseeing tech-related risks.

Corporate Culture and Ethical Leadership

In response to increasing public scrutiny and global calls for responsible business practices, companies will face increased pressure to demonstrate a values-driven culture. In 2025, further emphasis on creating strong ethical guidelines for companies to adhere to can be expected, with a focus on improving corporate accountability and maintaining trust with stakeholders. This could include more comprehensive training programmes for directors and executives, as well as improved mechanisms for reporting unethical behaviour.

Shareholder Engagement and Activism

Shareholder activism is likely to continue shaping corporate governance practices in 2025, especially as investors seek more influence over company strategies, including decisions related to corporate sustainability, executive compensation and strategic direction. Publicly traded companies may need to enhance their engagement

with shareholders to address concerns proactively, fostering a more collaborative relationship between shareholders and management.

2.2 ESG Considerations

As ESG considerations gain prominence in Malaysia's corporate landscape, companies are now expected not only to integrate these factors into their business practices and disclosures but also to disclose them transparently. This shift aligns with growing stakeholder demands and regulatory emphasis on sustainable, ethical business practices.

Environmental Reporting

Companies are required to disclose the impact of their operations on the environment, including areas such as carbon emissions, energy consumption, waste management and water usage. These ESG disclosures should be aligned with globally recognised standards, including the Global Reporting Initiative and the Task Force on Climate-related Financial Disclosures. In Malaysia, Bursa Malaysia and the SC require public listed companies to clearly detail their strategies for managing environmental risks and reducing their environmental footprint.

Social Reporting

Social reporting focuses on a company's responsibility towards internal and external stakeholders. Companies are expected to report on key aspects such as labour and employment practices, diversity and inclusion, human rights and community engagement and impact. The Listing Requirements and the MCCG encourage companies to demonstrate their commitment to social responsibility by showcasing efforts to enhance employee welfare, foster diversity and contribute to community development.

Governance Reporting

Governance reporting pertains to a company's internal structures and decision-making processes. Companies must disclose information regarding the composition of their Board, leadership practices and measures to protect shareholder rights. This includes establishing internal controls, risk management frameworks, anti-corruption measures and whistle-blower policies. The MCCG provides specific governance requirements, including the need for independent directors and the formation of Board committees to uphold sound corporate governance practices and ensure integrity in corporate decisions.

Regulatory Frameworks and Reporting Standards

In Malaysia, companies are expected to adhere to both local and international ESG reporting standards. The Malaysian Financial Reporting Standards (MFRS) and the MCCG provide guidelines for these disclosures. Bursa Malaysia mandates that public listed companies include ESG information as part of their annual reports, ensuring transparency and accessibility for stakeholders. Additionally, many companies voluntarily align their ESG strategies with global initiatives such as the United Nations Sustainable Development Goals (SDGs), thereby demonstrating a broader commitment to global sustainability objectives.

Accountability and Transparency

Transparency is a critical component of ESG reporting. Companies must provide accurate, complete and verifiable information on their ESG performance, including both achievements and areas for improvement. As investor interest in ESG data grows, many companies are now opting for third-party assurance or audits to validate their disclosures and enhance credibility.

This practice fosters trust among investors, stakeholders and the general public, reinforcing the company's commitment to responsible and sustainable business practices.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

In Malaysia, corporate governance and management are structured around several key bodies, each with distinct roles and responsibilities to ensure accountability, transparency and long-term corporate success. These functions are governed primarily by CA 2016, the MCCG and, for public listed companies, the Listing Requirements.

The principal bodies and functions involved in corporate governance and management are as follows:

- the Board;
- the senior management team (SMT); and
- Board committees, namely the audit and risk management committee (ARMC), nominating committee (NC) and remuneration committee (RC) (collectively, the *"Board Committee"*).

3.2 Decisions Made by Particular Bodies

In Malaysia, corporate decision-making is structured to ensure accountability, transparency and strategic alignment, with specific responsibilities assigned to key governance bodies. While decision-making is collaborative, certain types of decisions are exclusively reserved for particular bodies to safeguard the company's integrity and ensure sound corporate governance.

Board

The Board holds ultimate responsibility for the strategic direction, corporate oversight and long-term success of the company. In line with Principle A, Part I of the MCCG, the Board integrates sustainability considerations into corporate strategy and maintains collective accountability for governance outcomes. It oversees senior management, ensures regulatory compliance and fosters ethical leadership and good governance. Key responsibilities include approving major decisions, appointing and removing executives, and supervising financial performance. Directors are also expected to exercise professional scepticism and address evolving ESG risks to maintain stakeholder confidence and achieve long-term resilience.

SMT

The SMT, led by the chief executive officer (CEO) and/or managing director (MD), is responsible for executing the strategic initiatives and operational plans approved by the Board. The SMT manages the company's core functions, including finance, operations, marketing, human resources and legal affairs, and is accountable to the Board for achieving corporate goals and sustainable value for shareholders. As per Guidance 4.4 of the MCCG, performance evaluations of the Board and SMT should consider their role in addressing sustainability risks and progress on sustainability targets, promoting accountability and ensuring that issues are addressed and shareholders are kept informed of the outcomes.

Board Committee

The ARMC is responsible for reviewing and approving financial statements, overseeing internal and external audits and ensuring effective internal controls and risk management frameworks. The NC focuses on Board composition and effectiveness by making decisions

on the nomination, re-election and performance evaluation of directors, as well as succession planning. Meanwhile, the RC is entrusted with developing and reviewing policies related to executive remuneration, assessing executive performance and determining appropriate compensation packages. Together, the Board Committee ensures accountability, transparency and integrity in governance practices.

Collaborative Governance Framework for Effective Decision-Making

While each governance body operates within defined parameters, effective governance is achieved through collaborative efforts. The integration of functions between the Board, SMT and Board Committee ensures that decisions are made in a transparent, accountable and well-informed manner. This cohesive governance framework supports the company's commitment to regulatory compliance, ethical conduct and long-term value creation for stakeholders.

3.3 Decision-Making Processes

Board

The Board serve as the apex decision-making body, entrusted with setting the company's strategic direction, overseeing financial and operational performance and ensuring compliance with legal and ethical standards.

The decision-making process typically begins with the distribution of relevant documentation, including financial reports, strategic proposals and risk assessments, to directors prior to Board meetings to enable informed deliberation.

Formal Board meetings are then convened, during which directors discuss and deliberate on the matters tabled in the agenda. Decisions are made through collective agreement or formal voting, where required, and directors are expect-

ed to act with due care, skill and diligence, in line with their fiduciary duties as stipulated in Section 213 of CA 2016. Post-decision, the Board monitors the implementation of its directives, ensuring alignment with the company's objectives and compliance requirements.

The MCCG emphasises that the Board is collectively responsible for the company's long-term success and the delivery of sustainable value to stakeholders. Following Principle A, Part I of the MCCG, the Board is to set the company's strategic aims, ensure necessary resources are in place and oversee management performance.

SMT

Led by the CEO or MD, the SMT is responsible for implementing the Board's strategic decisions and managing the company's day-to-day operations.

This includes overseeing key areas such as finance, operations, marketing, legal affairs and human resources. SMT members exercise decision-making authority within their designated functions and operate under policies and limits defined by the Board.

Strategic planning is typically developed through collaboration within the SMT, ensuring alignment with the company's objectives. For complex matters, SMT members may consult with department heads or external advisors to enhance the decision-making process. Regular communication with the Board is maintained through periodic reporting and presentations to ensure transparency and strategic alignment.

Practice G4.4 of the MCCG recommends that performance evaluations of the Board and the SMT include reviews of their effectiveness in managing material sustainability risks

and opportunities. This practice emphasises the importance of integrating ESG considerations into the company's strategic and operational activities. This aligns with Section 211 of CA 2016, which allows the Board to delegate authority, while holding the SMT accountable for operational execution.

Board Committee

During committee meetings, the committee members review relevant information, which is often provided by management, internal auditors, external auditors or consultants. Committee members deliberate on the issues at hand, request further clarification where necessary and consult experts if appropriate.

Rather than making binding decisions, committees typically formulate recommendations or proposals for the Board's consideration. These recommendations are then reported to the full Board by the committee chairperson at scheduled Board meetings.

4. Directors and Officers

4.1 Board Structure

In Malaysia, the structure of a Board is designed to ensure accountability, effective oversight and sound corporate governance. A typical board structure includes:

- the chairperson of the Board ("*chairperson*")
- executive directors (EDs);
- non-executive directors (independent and non-independent) (non-EDs); and
- the Board Committee.

4.2 Roles of Board Members

Chairperson

The chairperson leads the Board by setting agendas, facilitating meetings and ensuring effective corporate governance. They act as a liaison between the Board and management, uphold high ethical standards and guide strategic decision-making, fostering a culture of accountability and integrity.

EDs

EDs are members of the Board who are also part of the company's management team. They are involved in the day-to-day running of the business and provide valuable insights based on their specific areas of expertise. Their contributions are vital in shaping and implementing the company's strategies.

Non-EDs

In contrast, non-EDs do not engage in the daily operations of the company but provide governance and oversight from a different perspective. They participate in Board meetings and decision-making processes, contributing their independent judgment to ensure that the company operates effectively and aligns with its long-term objectives. Independent directors play a critical role in safeguarding the interests of minority shareholders and maintaining the integrity of the Board. Their impartiality and objectivity bring balance to Board discussions and decision-making, particularly when handling matters such as corporate governance and risk management. Independent directors are crucial in enhancing the Board's transparency and accountability.

Board Committee

The Board Committee comprises specialised subgroups within the Board – ie, the ARMC, NC and RC – established to focus on specific areas of governance and decision-making. Its

primary role is to enhance the Board's efficiency by bringing close attention to complex issues, thereby supporting effective oversight and strategic guidance. Committee members bring specialised expertise to their respective committees, contributing to effective governance and ensuring that the Board functions smoothly in line with best practices. Each Board Committee subgroup is governed by written terms of reference, and they meet regularly to address their specific functions.

4.3 Board Composition Requirements/ Recommendations

In Malaysia, the composition requirements for the Board are primarily guided by the CA 2016, the MCCG and the Listing Requirements. These regulations aim to promote good corporate governance, transparency and accountability. The key composition requirements and recommendations follow.

Number of Directors

Pursuant to Section 196 of CA 2016, a company is required to have a minimum number of directors. In the case of a private company, the minimum requirement is one director, whereas in the case of a public company, the minimum requirement is two directors. Each director must be a natural person who is at least 18 years of age and must ordinarily reside in Malaysia, with a principal place of residence in the country.

Paragraph 15.02 of the Listing Requirements states that a public listed company must ensure that at least one-third of its Board, or a minimum of two directors, whichever is larger, be independent directors. If the number of directors is not divisible by three, the nearest whole number to one-third shall be used to determine the required number of independent directors. In the event of a vacancy on the Board that caus-

es non-compliance with these requirements, it must be filled within three months to ensure compliance.

Gender Diversity of Directors

Pursuant to paragraph 15.02 of the Listing Requirements, it is a mandatory requirement for public listed companies to ensure gender diversity in the Board by appointing at least one female director. In alignment with this, paragraph G5.9 of the MCCG recommends that every Board should comprise at least 30% women directors. Where the representation of women on the Board is below 30%, the Board is expected to disclose the actions it has taken or intends to take, along with a specific timeframe, typically within three years, to achieve the recommended threshold. Boards are also encouraged to review the participation of women in senior management positions to ensure a robust and sustainable talent pipeline for future leadership roles.

Tenure of Directors

Pursuant to Section 205 of CA 2016, in the absence of any specific provision in a company's constitution (formerly known as memorandum and articles of association) (the "*Constitution*"), all directors of a public listed company shall retire at the conclusion of its first annual general meeting (AGM). At each subsequent AGM, one-third of the directors shall retire, including those who have been in office the longest since their last appointment or reappointment. Notwithstanding the foregoing, retiring directors are eligible for re-election.

In terms of the tenure of independent directors, Principle A, Part II of the MCCG recommends that such tenure should not exceed a cumulative term limit of nine years. Upon reaching this limit, an independent director may continue to serve only in the capacity of a non-independent direc-

tor on the Board. If the Board intends to retain the individual as an independent director beyond the nine-year limit, it must provide a clear justification and seek annual shareholders' approval through a two-tier voting process.

Diverse Skills and Training of Directors

In accordance with the MCCG, the appointment of the Board should be based on objective criteria and merit, considering diversity in skills, experience, age, cultural background and gender. Boards are encouraged to ensure a composition with a broad range of competencies, including financial expertise, industry knowledge, legal proficiency, technological capabilities and strategic planning experience. To maintain effective governance, companies should regularly assess the collective qualifications and competencies of their Board members to ensure the Board is adequately equipped to discharge its responsibilities effectively.

Pursuant to paragraph 15.08 of the Listing Requirements, all directors of public listed companies are required to attend mandatory training programmes, as prescribed by Bursa Malaysia, to enhance their knowledge, professionalism and governance capabilities, thereby enabling them to effectively contribute to the oversight and strategic direction of the company.

Effective from 1 August 2023, all first-time directors of a new listed or transferred company must complete the Mandatory Accreditation Programme (MAP) Part II: Leading for Impact (LIP) within 18 months of appointment or admission to the company. Existing directors of listed companies have been required to complete the LIP within 24 months since 1 August 2023.

4.4 Appointment and Removal of Directors/Officers

In Malaysia, the appointment and removal of directors and officers are governed by CA 2016, the company's Constitution and, for public listed companies, the Listing Requirements.

Appointment of Directors/Officers

For private companies, the appointment of directors is usually a straightforward process. Pursuant to Section 202 (1) of CA 2016, individuals named as directors during a company's incorporation assume their roles from the date of incorporation. Subsequent directors can be nominated by shareholders via ordinary resolution under Section 202 (2) of CA 2016, or by the Board if permitted by the company's Constitution.

For public listed companies, directors are generally appointed by shareholders at general meetings or via written resolutions, in accordance with the company's Constitution, CA 2016 and the Listing Requirements. Section 203 of CA 2016 mandates that appointments of two or more directors must be voted on individually, reinforcing transparency and preventing block appointments. Any resolution passed contrary to this is void.

Removal of Directors/Officers

Pursuant to Section 206 of CA 2016, directors of both private and public listed companies may be removed by shareholders through an ordinary resolution. This power applies regardless of any contrary provision in the company's Constitution or a director's service contract, thereby preserving shareholder control. However, a special notice is required for any resolution to remove a director or appoint a replacement at the same meeting, and if a director represents a specific class of shareholders or debenture holders, the

removal does not take effect until a successor is appointed.

Eligibility and Restrictions

Notably, not all individuals are eligible to be appointed as directors. Under Section 198 of CA 2016, a person is disqualified if he/she is an undischarged bankrupt, convicted of offences involving fraud or dishonesty or convicted under CA 2016. Additionally, a director must be at least 18 years old and of sound mind, and must provide written consent to act. Directors of public listed companies are further restricted to holding no more than five directorships under the Listing Requirements.

4.5 Rules/Requirements Concerning Independence of Directors

In Malaysia, the independence of directors and the management of potential conflicts of interest are primarily governed by CA 2016, the MCCG and the Listing Requirements, as well as the prospectus guidelines issued by the SC (the "*Prospectus Guidelines*").

Pursuant to paragraph 1.01 of the Listing Requirements, an independent director is one who is independent of management and free from any business or other relationships that could interfere with the exercise of independent judgment or the ability to act in the best interests of an applicant or a listed issuer.

The MCCG further outlines criteria for independence, which include the absence of:

- any material shareholding or business relationship with the company;
- recent employment or executive positions within the company; and
- close family ties with directors, major shareholders or senior management.

Independent directors are also required to make annual declarations affirming their continuing independence. The MCCG recommends a cumulative tenure limit of nine years for independent directors, beyond which shareholder approval is required for continued service.

In the event where there are any conflicts of interest, Sections 219 and 221 of CA 2016 mandate directors to disclose any direct or indirect interest in contracts involving the company. Pursuant to Section 222 of CA 2016, directors with conflicts are required to abstain from voting or participating in the relevant decision-making process.

For prospectus disclosure, paragraph 8.01 of the Prospectus Guidelines mandates disclosure of any interests directors or substantial shareholders have in entities that compete or transact with the company, including the nature and extent of the interest, and steps taken to address or mitigate the conflict of interest.

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors and officers are primarily governed by CA 2016 and grounded in fiduciary and statutory responsibilities. These duties aim to ensure that directors always act in the best interests of the company and uphold proper standards of corporate governance. The core duties include the following.

Duty to Act in Good Faith

Pursuant to Section 213 (1) of CA 2016, directors are required to exercise their powers in good faith and in the best interests of the company. This duty mandates honesty and the prioritisation of the company's interest over personal or third-party interests. Directors must not misuse their position or any confidential information

obtained in their capacity, as further outlined in Section 218 (1)(e)–(f) of CA 2016.

Duty to Exercise Reasonable Care, Skill and Diligence

Pursuant to Section 213 (2) of CA 2016, directors must perform their roles with a reasonable degree of care, skill and diligence. This duty includes staying informed about the company's operations, actively participating in board meetings and making well-informed decisions. Directors are expected to apply their personal expertise and experience to the best of their ability.

Duty to Avoid Conflicts of Interest

Directors must avoid situations where their personal interests might conflict with the company's interests. Sections 219 and 221 of CA 2016 impose a duty to disclose any direct or indirect interest in transactions or matters relating to the company. Transparency and integrity are crucial in maintaining stakeholder trust.

Duty to Disclose

Directors are obligated to provide accurate, timely and complete disclosures of information to shareholders, regulators and other stakeholders. This includes ensuring that financial statements, annual reports and other disclosures comply with applicable accounting standards and regulatory requirements.

Duty to Act for Proper Purpose

Directors must exercise their powers only for legitimate and proper purposes, and not for any collateral or improper objectives. This duty ensures that all decisions are aligned with the company's Constitution and broader corporate objectives, rather than serving personal agendas.

Duty to Implement Adequate Procedures To Prevent Corrupt Practices

Section 17A of the Malaysian Anti-Corruption Commission Act 2009 (MACCA) imposed a duty on directors to ensure that the company establishes an adequate procedure to reasonably protect the directors and the company from liabilities under the MACCA.

Duty to Prevent Exposure to Anti-Money Laundering Activities

Directors must adopt policies and procedures consistent with the principles set out under the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLA), and there is also a duty to keep shareholders and employees abreast of matters under the AMLA. Directors must also remain vigilant against undertaking any business transaction that may be connected with or facilitate money laundering/terrorism financing.

4.7 Responsibility/Accountability of Directors

Directors owe their primary legal duties to the company. However, in discharging these duties, directors are also required to consider the interests of various stakeholders. In Malaysia, directors owe their duties to:

- the shareholders of the company – directors have a fiduciary duty to act in the best interests of the company's shareholders as a whole;
- the creditors of the company – directors shall manage the company's financial affairs prudently to safeguard creditors' interest, especially in situations of financial distress or insolvency;
- the stakeholders, including employees, customers and suppliers of the company – directors shall ensure fair labour practices, ensur-

ing product safety and quality, maintaining ethical supply chain standards and contributing positively to community development as recommended by the MCCG; and

- the community and environment – directors are expected to be mindful of the company's impact on the natural environment, including issues such as resource usage, pollution control, carbon footprint and compliance with environmental regulations.

4.8 Consequences and Enforcement of Breach of Directors' Duties

In Malaysia, enforcement of directors' duties is primarily the responsibility of the company itself. However, when the company fails to act, the shareholders of the company and regulators such as the CCM can intervene.

Pursuant to Section 347 of CA 2016, a shareholder (or other complainant) may, with the court's leave, initiate a derivative action on behalf of the company against a director who has breached their duties. This process requires giving 30 days' written notice to the company's directors, outlining the intention to apply for such leave.

In addition, regulators also play a significant role, particularly where a breach involves non-compliance with statutory obligations or raises issues of public interest. The CCM has the authority to investigate and prosecute directors for offences under CA 2016, including breaches involving dishonesty, negligence or abuse of power. For public listed companies, enforcement may also be undertaken by the SC or Bursa Malaysia, particularly in respect of contraventions of the Listing Requirements.

The consequences of breaching directors' duties may be both civil and criminal in nature. A direc-

tor found in breach may be held personally liable to compensate the company or to account for any gain obtained through misconduct. Where the breach involves fraud, dishonesty or gross negligence, criminal sanctions may apply. Pursuant to Section 213 (3) of CA 2016, a director who fails to act in good faith or for a proper purpose shall be subject to a fine not exceeding RM3 million, imprisonment of up to five years or both.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

There are various legal avenues through which directors and officers may be held liable for breaches of corporate governance standards, as follows.

Breach of Statutory Duties

Directors and officers may be held liable for breaching statutory duties imposed under CA 2016, securities laws and other relevant regulations. These obligations include the duty to ensure accurate and timely corporate filings, the maintenance of proper financial disclosures and the declaration of directors' interests as and when required.

Breach of Fiduciary Duties

Directors are bound by fiduciary duties to act in good faith, exercise reasonable care and diligence and act in the best interests of the company. A breach of fiduciary duty may give rise to civil proceedings initiated by the company, shareholders or other affected stakeholders.

Negligence Under Tort Law

Directors and officers may also face liability under the law of tort for negligence in the performance of their corporate duties. This applies when they fail to act with the level of care, skill or diligence that a reasonable person would exer-

cise in similar circumstances. Negligence may arise from poor oversight, lack of proper governance or failure to detect and prevent operational or financial misconduct.

Fraud or Misrepresentation

Directors who engage in fraudulent activities or misrepresentation of information may be subject to legal actions and penalties.

Corrupt Practices

Directors who fail to establish an adequate procedure that can be used to reasonably protect the directors and the company from liabilities under the MACCA may be subject to legal actions and penalties.

Anti-Money Laundering Activities

Directors who fail to adopt policies and procedures in line with the principles set out under the AMLA may be subject to legal actions and penalties.

In Malaysia, there are limited circumstances in which the director or officer's liability can be limited. The company may indemnify directors or officers for liabilities incurred in the course of performing their duties, provided that the indemnification is permitted under the company's Constitution and the indemnity does not extend to fraud, dishonesty or wilful misconduct.

Furthermore, directors may also seek directors' and officers' (D&O) liability insurance as an added layer of protection, covering liabilities incurred in their official capacity subject to legal limitations. CA 2016 also provides certain statutory protections that may limit the personal liability of directors or officers under specific circumstances. These include the business judgment rule, which protects directors from liability for decisions made in good faith, with reasonable

care and in the best interests of the company. Additionally, CA 2016 empowers the court to grant relief from liability where it is satisfied that the director has acted honestly and reasonably.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

In Malaysia, remuneration, fees and benefits payable to directors and officers of a company, as well as loans to directors, are subject to approval requirements and restrictions that are primarily governed by CA 2016 and regulations issued by regulatory bodies such as Bursa Malaysia.

Pursuant to Section 224 of CA 2016, a company shall not make a loan to a director of the company or of a company deemed to be related to that company, nor shall it enter into any guarantee or provide any security in connection with a loan made to such a director by any other person.

By virtue of Section 225 of CA 2016, subject to certain provisions, a company (other than an exempt private company) shall not make a loan to any person connected with a director of the company or its holding company, nor enter into any guarantee or provide any security in connection with a loan made to such person by any other person. Nevertheless, this shall not apply to, amongst others, loans made to a person connected with a director who is engaged in the full-time employment of a company or its related corporation, as the case may be, (i) for the purpose of meeting the expenditure incurred or to be incurred by him or her in purchasing or otherwise acquiring a home or (ii) in accordance with a scheme for the making of loans to employees approved by the company.

Pursuant to Section 226 of CA 2016, a company shall not pay a director any remuneration free

of income tax, or otherwise calculated by reference to or varying with the amount of his or her income tax or the rate of income tax.

Furthermore, Section 230 of CA 2016 provides that the fees of the directors, and any benefits payable to the directors (including any compensation for loss of employment of a director or former director of a public company, or of a public listed company and its subsidiaries) shall be approved at a general meeting. As for a private company, the Board may, subject to the company's Constitution, approve the fees of the directors and any benefits payable to the directors, including any compensation for loss of employment of a director or former director. Contravention of the same constitutes an offence for which, upon conviction, the company and/or its officers will be liable to imprisonment, a fine or both, where the figures relies on the specific contravention.

4.11 Disclosure of Payments to Directors/Officers

In Malaysia, companies must publicly disclose details about the remuneration, fees and benefits provided to directors and officers. The purpose of such disclosure is to promote transparency for shareholders and stakeholders, ensuring accountability in corporate governance. CA 2016, the Listing Requirements and the MCGG outline such obligations.

Pursuant to Section 219 (1) of CA 2016, a director shall give notice in writing to the company of, inter alia, the following:

- particulars relating to the shares, debentures, participatory interests, rights, options and contracts as necessary;
- the particulars of any change in respect of the particulars aforesaid of which notice has been

given, including the consideration, if any, received as a result of the event giving rise to the change; and

- such events and matters affecting or relating to the director as necessary for compliance with CA 2016.

In respect of public listed companies, Section 232 (1) of CA 2016 requires a public company to keep and maintain a copy of every director's service contract with the company – or with its subsidiaries – available for inspection, where such service contract is defined as, as per Section 231 of CA 2016, a contract under which (i) the director of the company undertakes personally to perform services, as a director or otherwise for the public company or for a subsidiary of the public company, or (ii) services are performed by a director of the public company or are otherwise made available via a third party to the public company, or to a subsidiary thereof.

Further to the foregoing, a company's directors are required to prepare a directors' report for each financial year, which must be attached to the financial statements in accordance with Section 252 of CA 2016. This report must detail, with clear distinction, the fees and other benefits received or receivable by the directors from the company or its subsidiaries as payment for their services.

Furthermore, publicly listed companies must provide comprehensive disclosures in their annual reports regarding the remuneration of their directors and officers pursuant to the Listing Requirements. This includes the total amounts paid or payable to each individual, covering items such as directors' fees, salaries, bonuses, commissions, benefits-in-kind and other forms of compensation.

Malaysian companies, especially those listed on Bursa Malaysia, are subject to stringent disclosure obligations concerning directors' and officers' remuneration. These measures are designed to uphold high standards of corporate governance and protect stakeholders' interests.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

By holding shares, shareholders are essentially the owners of a company, with rights and powers typically outlined in CA 2016 and the company's Constitution. Public listed companies are additionally subject to regulations and disclosure requirements enforced by the SC and Bursa Malaysia, ensuring transparency and protection of shareholders' interests. The MCCG further provides best practices for responsible management and stakeholder engagement.

The shareholders possess rights proportional to their shareholdings, such as receiving dividends declared by the company; attending, participating in and speaking at general meetings; and voting on significant matters – ie, appointing and removing directors. While shareholders hold ownership, the day-to-day management of the company is entrusted to the Board and executive officers, as mentioned in the foregoing.

In respect to the publicly available records of shareholders, companies are required to maintain a share register recording the names and shareholdings of all shareholders. Such information is also available in the company's annual return. For public listed companies, annual reports disclose the substantial shareholders (those holding 5% or more) and shareholders who also serve as directors. Furthermore,

the shareholdings of directors are disclosed in reports such as the company's audited financial statements (AFS). All of the aforesaid can be purchased through the official online platform, known as the CCM e-Info portal ("*CCM e-Info*"). Shareholders have the right to inspect the register of members without charge and may request copies for a prescribed fee.

5.2 Role of Shareholders in Company Management

In general, shareholders have limited involvement in the day-to-day management of a company. Instead, their role is more focused on oversight, governance and major decision-making, while the day-to-day operations are managed by the Board and executive management.

However, shareholders possess certain rights and mechanisms to influence company management in specific circumstances. Pursuant to Section 195 of CA 2016, the chairperson of a meeting of shareholders shall allow a reasonable opportunity for shareholders, present at the meeting, to question, discuss, comment on or make recommendations concerning the management of the company. Furthermore, a meeting of shareholders may pass resolutions, making recommendations to the Board on matters affecting the management of the company. However, it is to be noted that any such recommendation via resolution shall not be binding on the Board unless the right to make such recommendations is provided for in the company's Constitution or such recommendations are passed as a special resolution (requiring at least a 75% majority) and is in the best interest of the company.

Even when recommendations meet the foregoing criteria, the Board is obligated to act in the company's best interests. They must exercise

independent judgment and are not compelled to follow shareholder recommendations if doing so would conflict with their fiduciary duties.

5.3 Shareholder Meetings

Pursuant to Section 340 of CA 2016, every public company shall hold an AGM annually, within six months of the company's financial year end and no more than 15 months after the previous AGM, for the purposes of, inter alia, presenting the AFS and the reports of the directors and auditors, the election of directors and matters notified vide resolution.

Section 290 of CA 2016 allows for a resolution of the members, or of a class of members, of a private company to be passed either by a written resolution or at a meeting of the members. However, certain decisions, such as removal of a director or auditor, cannot be effected through written resolutions of the members and shall be addressed at a meeting of the members.

A meeting of members may be convened by the Board, or by members holding at least 10% of the issued share capital of a company or a lower percentage as specified in the company's Constitution – or, if the company has no share capital, by at least 5% of the members.

Prior to convening the meeting, a notice of at least 14 days is required for meetings of members of private companies except when passing a special resolution, which may require a longer period as stated in the company's Constitution. Meetings of members of public companies shall be by way of a notice of at least 21 days for AGMs and 14 days in any other meetings, unless a longer period is stipulated in the company's Constitution.

Should the members require the directors to convene a meeting of members pursuant to Section 311 of CA 2016, the directors shall call for the meeting within 14 days from the requisition and hold it within 28 days after the date of the notice, as provided under Section 312 of CA 2016. If the directors fails to do so, the members who requisitioned the meeting, or those representing more than half of the total voting rights of all of the members who requested the meeting, may convene the meeting of members, provided that it is held not more than three months after the requisition date.

In respect of the required quorum of the meetings, a minimum of one (in the case of a company only having one member) or two members would be required unless the company's Constitution requires otherwise (Section 328 of CA 2016). The chairperson shall be the person subjected to the company's Constitution. If there is no such person, or if the chairperson is not present within 15 minutes after the scheduled time or is unwilling to act, the members present shall elect one of their members to be chairperson of the meeting.

At any meeting of members, a resolution put to the vote of the meeting shall be decided on a show of hands unless a poll is demanded before or on the declaration of the result of the show of hands by the parties provided under Section 330 of CA 2016, which includes, inter alia, the chairperson or at least three members present in person or by proxy.

In respect of the records of the meeting, by virtue of Section 341 of CA 2016, all resolutions of members passed otherwise than at the meeting of members, the minutes of all proceedings of meetings of members and details provided to the company in accordance with Section 344 of CA 2016 shall be kept for at least seven

years from the date of said resolution, meeting or decision, whereby the same shall be kept at the registered office of the company pursuant to Section 47 of CA 2016.

5.4 Shareholder Claims

In respect of the available bases of claims against the directors of the company and/or the company itself, examples include breaches of fiduciary duties, oppressive conduct, unlawful appointment of directors and/or mismanagement. Actions in negligence, fraud or other breaches of duty owed to the company and/or its shareholders may qualify as well.

Pursuant to Section 346 of CA 2016, any member or debenture holder may apply to the court if:

- the company's affairs are being conducted, or the powers of the directors are being exercised, in an oppressive manner in relation to one or more of the members or debenture holders, or in disregard of their interests; or
- the company has or has threatened to act in a way – or some resolution of the members, debenture holders or any class of them has been passed, or even proposed – that unfairly discriminates against or is otherwise prejudicial to one or more of the members or debenture holders.

Section 347 of CA 2016 provides a statutory mechanism for a complainant – which could be a current or former shareholder of a company, any director of a company or the registrar in the case of a company being investigated – to initiate, intervene in or defend a proceeding on behalf of the company with the leave (permission) of the court. This is particularly relevant when the company fails to take action against wrongdoers, such as directors or majority shareholders.

The complainant shall give 30 days' notice in writing to the directors of his or her intention to apply for the leave of court, and an action should be initiated within 30 days where leave is granted. When deciding whether or not leave ought to be granted, the court will consider whether the complainant is acting in good faith, and whether it is in the best interest of the company. If leave is granted, the action is initiated in the company's name, and any settlement or discontinuance requires the court's approval.

This mechanism ensures that the company's interests are preserved, especially in situations where those in control are unwilling or unable to act against misconduct.

5.5 Disclosure by Shareholders in Publicly Traded Companies

In Malaysia, shareholders of publicly listed companies are subject to specific disclosure obligations.

Substantial Shareholding Disclosure

Under Section 137 of CA 2016, individuals or entities with shareholdings exceeding specific thresholds – namely, 5% or more of the company's voting rights – are required to notify the company and CCM in writing of any changes to their interest in the company's voting shares within three days from the date the change occurs. Failure to comply may result in fines of up to RM1 million and additional daily penalties for ongoing non-compliance.

Beneficial Ownership Reporting

The Companies (Amendment) Act 2024 introduced Section 60B into CA 2016, where every company must maintain a register of its beneficial owners and include their details in this register. This register must be kept either at the company's registered office or at another loca-

tion in Malaysia that has been notified to the CCM. Companies are required to lodge any changes to this information with the CCM within 14 days of the change. Additionally, companies must retain records of former beneficial owners for seven years after they cease to be beneficial owners. Failure to comply may result in fines of up to RM20,000 and additional daily penalties for ongoing non-compliance.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

In Malaysia, companies are subject to annual and periodic financial reporting requirements under CA 2016, with additional requirements for public listed companies under the Listing Requirements.

Private companies shall prepare financial statements and reports, circulate them to members and subsequently lodge them with the CCM. Under Section 68 of CA 2016, companies are required to lodge their annual returns with the CCM within 30 days from each anniversary of incorporation. This requirement does not apply to the calendar year of incorporation.

As for public listed companies, they shall present the financial statements and reports at their AGM and lodge them with the CCM. Similar to private companies, public listed companies must lodge their annual returns with the CCM within 30 days from the each anniversary of incorporation. This requirement is not applicable to the company in the calendar year in which it is incorporated. Extensions for lodgement may be granted by the CCM upon application by private and public listed companies.

In addition to the foregoing, public listed companies shall provide an interim financial report on a quarterly basis. These reports should be prepared as soon as the figures are approved by the Board and must be announced to Bursa Malaysia not later than two months after the end of each quarter of a financial year.

These reporting obligations are designed to ensure transparency, facilitate investor confidence and uphold corporate governance standards in Malaysia.

6.2 Disclosure of Corporate Governance Arrangements

In accordance with the Listing Requirements and MCCG, public listed companies are required to disclose their corporate governance arrangements in their annual reports. Companies shall provide an overview of the application of the principles set out in the MCCG during the financial year. Additionally, companies must submit a detailed corporate governance report to Bursa Malaysia, outlining the application of each MCCG practice including explanations for any departures and alternative measures adopted to achieve the intended outcomes.

Furthermore, to ensure transparency and ease of access for stakeholders, companies are also required to indicate in their annual report the specific website link or address where the full disclosure can be accessed or downloaded. Beyond compliance, companies are encouraged to view corporate governance disclosure as an opportunity to demonstrate to stakeholders that they have holistic and effective corporate governance arrangements.

6.3 Companies Registry Filings

In Malaysia, the primary body responsible for company incorporation, registration, regulation and supervision under CA 2016 is the CCM.

Private and public listed companies are required to make various filings with the CCM including, but not limited to, the notification of changes in directors or shareholders, the filing of annual returns, AFS and other disclosures mandated under CA 2016. Filings submitted to the CCM are generally accessible to the public through CCM e-Info.

Failure to comply with the statutory filing obligations within the prescribed timeframes may result in enforcement actions by the CCM, including the imposition of fines, compoundable offences or, in more severe cases, legal action against the company and its officers.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Under Section 271 of CA 2016, a company must appoint an external auditor at each AGM. The appointed external auditor holds office until the conclusion of the next AGM of the company. The person appointed shall not be an auditor of the company if, among other things, he or she, or his or her spouse, is an officer of the company, a partner, an employer or employee of an officer of the company, or a partner or employee of an employee of an officer of the company, or if they have certain shareholding interests that may impair independence.

Paragraph 15.21 of the Listing Requirements stipulates that a public listed company must consider, amongst other things, the following when appointing an external auditor:

- the adequacy of the experience and resources of the accounting firm;
- the persons assigned to the audit;
- the accounting firm's audit engagements;
- the size and complexity of the company's group; and
- the number and experience of supervisory and professional staff assigned to the audit.

The auditor must uphold high ethical standards throughout the audit process, ensuring objectivity, integrity and professionalism in their work.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Reviewing the effectiveness of risk management and internal control is an essential part of the directors' responsibilities and should be performed at least annually. Pursuant to paragraph 15.26 (b) of the Listing Requirements, the Board shall include in the company's annual report a

statement detailing the risk management and internal control systems of the public listed company as a group. The directors are required to form their own independent view on the effectiveness of governance and internal controls based on the information and assurances presented to them. In doing so, directors must exercise the standard of care, diligence and skill expected of them in fulfilling their fiduciary responsibilities.

Directors' responsibilities include:

- ensuring that risk management is embedded across all aspects of the company's activities;
- determining the company's risk appetite; and
- overseeing the adequacy of the risk management framework, including the underlying processes, roles and responsibilities, to determine whether they provide reasonable assurance that risks are managed within acceptable parameters and internal control systems.

Trends and Developments

Contributed by:

Dato' Tan Yee Boon, Stephanie Chan Pik Jia and Joaana Keng Li Xin

David Lai & Tan

David Lai & Tan is a reputable and dynamic law firm established in 2013 by Dato' Tan Yee Boon, Mr David Lai Chung Yew and Mr David Cheong. Based in Kuala Lumpur, Malaysia, the firm offers a full spectrum of legal services, focusing on both contentious and non-contentious corporate and commercial matters. With a dedicated team of experienced advocates and solicitors, David Lai & Tan serves a diverse clientele including public-listed companies, investment banks and multinational corporations. The firm is highly regarded for its practical, high-quality

and solution-oriented legal advice. David Lai & Tan has been consistently recognised by leading law directories, including Chambers Asia Pacific (2024–25) for corporate/commercial: equity capital markets. Key areas of expertise include initial public offerings (IPOs), mergers and acquisitions (M&As), corporate restructuring and shareholder disputes. Known for its partner-led approach and unwavering professionalism, the firm continues to uphold the highest standards of legal practice.

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The Malaysian Code on Corporate Governance (MCCG) underwent substantial revision in 2021 and remained the framework for companies in Malaysia to adopt internationally recognised practices. After the revision to the MCCG, the corporate governance landscape in Malaysia saw rapid growth, with the implementation of various other frameworks aimed at enhancing the attractiveness of Malaysia to foreign investors.

National Sustainability Reporting Framework (NSRF)

Introduced jointly by the Ministry of Finance and the Securities Commission (SC) on 24 September 2024, the NSRF laid down a disclosure framework in line with the International Financial Reporting Standards (IFRS) Sustainability Disclosure Standards issued by the International Sustainability Standards Board.

The NSRF adopted the General Requirements for Disclosure of Sustainability-related Financial Information (“IFRS S1”) and Climate-related Disclosures (“IFRS S2”) (collectively, the “IFRS Standards”). The NSRF is set to be implemented in phases from 2025 to 2030. Starting on 1 January 2025, the authors see the framework being implemented for entities listed on the main market of Bursa Malaysia Securities Berhad (“Bursa Malaysia”) with a market capitalisation of RM2.0 billion and above, while other main market-listed issuers will commence using the IFRS Standards in 2026. ACE market-listed issuers, as well as non-listed companies (NLCos), with annual revenue of RM2.0 billion and above will commence using the IFRS Standards in 2027.

On 23 December 2024, Bursa Malaysia introduced amendments to the main market listing requirements (MMLR) and the ACE market listing requirements (AMLR) to align the sustainability

reporting requirements under the MMLR and AMLR with the NSRF. The amendments adopted IFRS S1 and IFRS S2 and the publication of a sustainability statement in the annual report.

Amendments including the Sustainability Reporting Guide issued by Bursa Malaysia in 2022 also required the listed issuers to:

- make a statement regarding whether the sustainability statement had been reviewed by an internal auditor or whether independent assurance had been performed in accordance with recognised assurance standards, such as IFRS S1 and IFRS S2;
- specify a reporting metric to indicate the listed issuer’s performance and progress relating to its sustainability-related risks and opportunities in the last three financial years on a rolling basis, together with a summary of such data in a prescribed format;
- adopt, for issuers listed on the main market with a market capitalisation of less than RM2.0 billion, the IFRS Standards for annual reporting from 1 January 2025 onwards (from 1 January 2026 onwards for the remaining main market-listed issuers); and
- adopt, for issuers listed on the ACE market, the IFRS Standards for annual reporting from 1 January 2027 onwards.

However, full implementation of the NSRF will require amendments to relevant legislation, including inter alia the Financial Reporting Act 1997, Companies Act 2016, Capital Market and Services Act 2007 and other laws and regulations.

Policy, Assumptions, Calculators and Education (PACE) Initiative

To support companies in adopting the NSRF, the Advisory Committee on Sustainability Report-

ing of the SC introduced the PACE initiative, designed to help companies successfully adopt the NSRF. PACE offers policy guidance, assumptions, calculators and educational resources to assist companies, including those listed on the main and ACE markets, in complying with the NSRF and IFRS Standards.

Bursa Malaysia, on 24 September 2024, issued a public consultation paper regarding the consequential amendments to the MMLR and AMLR (collectively known as the “*Listing Requirements*”). The public consultation closed on 25 October 2024. To ensure that the Listing Requirements fit with the ongoing developments in the capital marker landscape, the following key amendments to the Listing Requirements have been proposed.

Adviser/sponsor disclosure requirement

One of the key amendments proposed to the MMLR and AMLR is the greater accountability of the advisers during the listing process. Specifically, companies listed on the main market are now required to disclose the name of the recognised principal adviser responsible for its listing, in all announcements to Bursa Malaysia and in documents issued to securities holders (public documents), for two full financial years from the date of listing. Similarly, companies listed on the ACE market must state the name of their listing sponsor in all public documents for at least three full financial years after its admission to the ACE market, or for at least one full financial year after the applicant has generated operating revenue, whichever is the later, under the AMLR.

These disclosures must be prominently displayed on the front page of the relevant documents, in print no smaller than the main text and positioned on the front page of the public documents. This initiative aims to strengthen the

accountability of advisers and sponsors, ensuring greater transparency and trust in the listing process.

Physical general meeting

An amendment was made to the MMLR and AMLR to require all listed issuers to hold their general meeting as a hybrid or physical meeting, effective from 1 March 2025. A trend towards virtual general meetings emerged after the implementation of the movement control order (MCO) implemented under the Prevention and Control of Infectious Diseases Act 1988.

Completely virtual general meetings became popular among listed issuers, but some held that such meetings had been abused to censor shareholders’ right to speak at a general meeting. Now, a general meeting must be held at a physical venue in Malaysia.

Governance Code for Malaysian Micro, Small and Medium Enterprises (MSMEs)

MSMEs are a cornerstone of the Malaysian economy, driving growth, innovation and employment across various sectors. In view of their critical role and the growing global emphasis on ESG principles, it is increasingly important for MSMEs to adopt strong governance practices to enhance transparency, uphold integrity and remain competitive in today’s evolving market landscape.

The SME Governance Working Group, chaired by the SC and participated in by the Ministry of Entrepreneur and Cooperative Development (MECD), SME Corporation Malaysia and the Malaysian Institute of Corporate Governance, issued the draft Governance Code for MSMEs (the “*Code*”) for public consultation. The Code focuses specifically on governance practices, including those required to ensure there is clear

accountability for decision-making related to the management of the sustainability risks and opportunities of the company. The Code comprises five fundamental principles, including decision-making and strategic oversight; culture and commitments; risk governance and internal controls; sustainability, disclosure and transparency; and data protection.

Expanding the Scope of Disclosure for Conflict of Interest Involving a Director

Bursa Malaysia amended the MMLR and AMLR, requiring the disclosure of any conflict of interest involving a director to include the nature and extent of such conflict of interests, as well as disclosure of potential conflicts of interest relating to interest in any competing business.

Further Transparency in New Issue of Securities

Bursa Malaysia's amendment of the MMLR and AMLR also required a listed issuer, effective as of 2 January 2025, to:

- disclose, on a quarterly basis, the price issuance date, issuance date, number of securities issued and/or allotted and the issue price, including the basis of price fixing for a staggered issuance of securities;
- submit, to Bursa Malaysia, the source of funds for the payment by each "place", including the details of any beneficial owner of such securities; and
- disclose the remuneration of chief executives in the annual report.

The amendments also imposed an upper limit of 50% of the issued shares of a listed issuer for any convertible debt securities, and extended the chain listing requirement to a listed issuer who wishes to list its subsidiaries on a foreign stock exchange.

Under Practice Note 17 of the MMLR and Guidance Note 3 of the AMLR, an affected issuer is not prohibited from undertaking any interim corporate proposal prior to its regularisation plan, unless such interim corporate proposal is allowed by Bursa Malaysia.

Code of Ethics for Company Director and Company Secretary (the "Code of Ethics")

The company director and company secretary roles are key to ensure legal compliance, accurate records, effective shareholder communication, risk management, sound governance and transparent operations. The Companies Commission of Malaysia (CCM) issued the Code of Ethics on 11 September 2023, which came into force on 1 January 2024. The Code of Ethics was formulated to enhance corporate governance and corporate behaviour, with a view to achieving the following objectives:

- establishing standards of ethical conduct for company directors based on the acceptable beliefs and values one upholds;
- upholding the spirit of accountability and transparency in line with the legislations, regulations and guidelines governing a company; and
- promoting the sustainability of a company by pursuing ESG strategies in its business.

The Companies (Amendment) Act 2024 (the "Amendment Act") – Reporting of Beneficial Ownership Information

The Amendment Act, which came into force on 1 April 2024, establishes a robust framework for the reporting of beneficial ownership in Malaysia, aimed at strengthening corporate transparency and meeting international standards and practices, such as those of the Financial Action Task Force (FATF) and the Organisation for Economic Co-Operation and Development (OECD). The

main objective of those standards is to combat money laundering, terrorist financing and other illegal activities, such as corruption and tax evasion.

Following the implementation of the Amendment Act, companies (including the board of directors, company secretaries, agents, members of the company and any person who received any notice under Section 60C of the Companies Act 2016) are now required to proactively identify and verify their beneficial owners (pursuant to Section 60A of the Companies Act 2016, a beneficial owner is defined as an individual or natural person who ultimately owns or controls a company, including the person who exercises ultimate effective control over a company). Each company shall also maintain a register of beneficial owners at their registered office and report changes to the CCM within a stipulated timeframe.

This beneficial ownership reporting framework aims to include persons with no shares in the company but who ultimately have control over the company. Together with the guidelines issued by the CCM, it is applicable to all companies (including foreign companies) that are incorporated and registered under the Companies Act 2016.

MEXICO



Law and Practice

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Aziz & Kaye Abogados, S.C. is headquartered in Mexico City. The firm serves as a strategic ally and gateway for doing business in Mexico. Its mission is to provide bespoke legal advice, delivering value to companies seeking top-tier professionals with strong legal expertise and a business-oriented approach to decision-making. Specialising in corporate, transactional, financial, and antitrust law, Aziz & Kaye navigates the complex legal and commercial landscapes of its clients. With two partners, one of counsel

and six associates, the corporate team draws on over three decades of experience, offering expert advice on M&A, joint ventures, due diligence, corporate governance, foreign investment, and global relocation (nearshoring). Its corporate clients operate across a range of industries including real estate, banking, entertainment, healthcare, advertising, transportation, and telecommunications, with a client base that includes publicly listed companies in both Mexico and the US.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The main business organisations in Mexico are governed by the General Law of Business Companies (*Ley General de Sociedades Mercantiles*) and are as follows:

- limited liability companies (*sociedad de responsabilidad limitada*);
- corporations (*sociedad anónima*);
- general partnerships (*sociedad en nombre colectivo*);
- limited partnerships (*sociedad en comandita simple*);
- limited joint-stock partnerships (*sociedad en comandita por acciones*);
- cooperative companies (*sociedad cooperativa*); and
- simplified corporations (*sociedad por acciones simplificada*).

Any of these may be incorporated or converted into a variable capital company, in which case the company must add the words “of variable capital stock” (“*de capital variable*”) to its cor-

porate name. Variable capital companies are typically preferred as there are fewer formalities involved in adjusting the variable portion of their capital stock.

Limited liability companies and corporations are the most common form of business organisations for conducting business in Mexico.

Limited Liability Companies

Two or more partners can set up a limited liability company, but the number of partners must not exceed 50. The partners in a limited liability company are liable only to the extent of their equity contribution. Any person who is not a partner but allows the use of their name in the name of the company is liable for the company’s transactions up to an amount equal to the largest equity contribution in the company.

Equity interests are not represented by stock certificates, nor are they freely transferable. The admission of new partners and any assignment or transfer of equity interests must be approved by the partners representing at least the majority of the capital stock, unless the company’s by-laws provide for a higher proportion. In general,

such consent is not required when an equity interest is transferred by inheritance.

The partners have a right of first refusal if any other partner transfers equity shares. Should several partners intend to exercise this right, it will be exercised in proportion to their contributions.

Limited liability companies are required to keep a Special Partners Book that details the name, address, contributions, and taxpayer registry number of each partner and any transfer of their equity interests. Transfers are only effective upon registry in this book, and a notice of the registry will be published on an electronic platform operated by the Ministry of the Economy.

In practice, limited liability companies may also keep a Book of Minutes of Partners' Meetings, a Book of Variations to Capital Stock, and a Book of the Board of Managers' Meetings.

Given that a limited liability company may qualify as a pass-through entity for US tax purposes, US companies frequently use this type of company as a subsidiary in Mexico.

Corporations

Corporations are regulated by the General Law of Business Companies. However, they may adopt the form of a promotion investment corporation (*sociedad anónima promotora de inversión*, or SAPI), which is also regulated by the Securities Market Law (*Ley del Mercado de Valores*).

Companies with shares that are publicly traded are incorporated as corporations. These may either be a stock corporation (*sociedad anónima bursátil* or SAB) or a stock promotion investment corporation (*sociedad anónima promotora de inversión bursátil*, or SAPIB). See 1.3 Corporate

Governance Requirements for Companies With Publicly Traded Shares for more information. However, under the recently created framework for simplified issuers, entities seeking to issue equity securities through this simplified mechanism must be a SAPIB. See 2.1 Hot Topics in Corporate Governance for more information.

Corporations are formed by two or more shareholders whose liability is limited to the payment of their shares. Such shares are represented by certificates that are freely transferable unless otherwise provided for in the company's by-laws or a shareholders' agreement.

Corporations are required to keep a Book of Minutes of Shareholders' Meetings, a Book of Variations to Capital Stock, and a Share Registry Book. The Share Registry Book must contain, among other items, the name, address, nationality, and taxpayer registry number of the shareholders, details on the shares held by each shareholder, and the contribution payments and transfers made.

Transfers of shares are effective upon the endorsement of the share certificate to the acquirer and the registry of the transfer in the Share Registry Book. A notice of such registry shall be published on an electronic platform operated by the Ministry of the Economy.

In practice, some corporations governed by a board of directors choose to maintain a corporate book documenting the meetings of this governing body.

According to the General Law of Business Companies, the shareholders of corporations have certain minority rights, such as the following.

- When the board of directors or the surveillance body is comprised of three or more members, shareholders may appoint a member of the board or a statutory auditor, as applicable, if they hold 25% or more of the capital stock.
- Shareholders holding at least 33% of the capital stock may call a shareholders' meeting.
- Shareholders that own 25% or more of the capital stock may: (i) exercise a liability action against directors; (ii) delay the voting on an issue; and (iii) judicially oppose a resolution adopted by the general shareholders' meeting.

Promotion Investment Corporations

Promotion investment corporations (SAPI) are companies regulated by the Securities Market Law and the General Law of Business Companies. The SAPI was created to promote capital risk investments by providing more flexibility to agree on several issues that were considered relevant for investors and granting minority rights with a lower participation percentage.

As stated, a SAPI is a variation on a regular corporation. Several amendments to the regulation of corporations have reduced the number of differences between both types of entities.

However, there are still some relevant distinctions between them, as follows:

- SAPIs are allowed to acquire their shares; corporations are not allowed to carry out such acquisitions, except in the case of judicial adjudication for the payment of the company's debts; and
- SAPIs are managed by a board of directors; corporations may be managed by a board of directors or a sole manager.

Shareholders in a SAPI may:

appoint a member of the board of directors or statutory auditors for each 10% of the voting shares held individually or in aggregate, even if voting rights are limited or restricted;

- if they hold at least 10% of the capital stock of the company, call a general shareholders' meeting;
- if they hold 15% or more of the shares with voting rights (even if limited or restricted) or without voting rights, exercise a liability action against the directors;
- if they hold 10% or more of the capital stock of the company, delay voting on a specific issue; and
- if they hold 20% or more of the capital stock of the company, judicially oppose a resolution adopted by the general shareholders' meeting.

Shareholders in corporations cannot be excluded from profit sharing. SAPI may issue shares with special rights regarding profit sharing and other economic rights that expand or limit the shareholders' rights over profits.

1.2 Sources of Corporate Governance Requirements

Corporate governance requirements are outlined mainly in the General Law of Business Companies and, for the SAPI, SAB and SAPIB, in the Securities Market Law. The laws apply at federal level and to all companies in Mexico, irrespective of the state of incorporation of the company.

Corporate governance requirements are also outlined in the companies' corresponding by-laws and, when applicable, in shareholder agreements.

For entities whose operations are subject to governmental approval, certain corporate governance requirements may be prescribed by the relevant regulatory framework.

For example, multiple-purpose financial companies (*sociedades financieras de objeto múltiple*, or SOFOMs), besides complying with the General Law of Business Companies (and the Securities Market Law if the SOFOM is also a SAPI), must comply with the requirements of corporate name and corporate purpose set forth in the General Act on Credit Organisations and Related Activities (*Ley General de Organizaciones y Actividades Auxiliares del Crédito*).

Certain corporate requirements may also be found in tax legislation. For example, the Federal Fiscal Code (*Código Fiscal de la Federación*) states that the shareholders' taxpayer registry number must be annotated in the Special Partners or Share Registry Books, as applicable. Furthermore, companies are also obliged to file a notice before the tax authorities on any change of partners or shareholders.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with shares that are publicly traded must comply with the corporate governance provisions of their by-laws, the Securities Market Law and, in the absence of a specific rule, the provisions of the General Law of Business Companies.

As discussed in **1.1 Forms of Corporate/Business Organisations**, there are two types of companies whose shares can be publicly traded, the SAB and the SAPIB.

The shareholders of SABs are entitled to minority rights, including the following.

- For each 10% of the capital stock granting them the right to vote, even if on a limited or restricted basis, they may: (i) appoint one member of the board of directors; (ii) request a general shareholders' meeting; and (iii) request a delay (once and only for three days) on the voting of any matter on which they consider they have not received adequate information.
- When holding 20% or more of the capital stock with the right to vote (even if their vote is restricted or limited), they may judicially oppose the resolutions of the general shareholders' meetings to the extent they have the right to vote over such resolutions.

In addition, the shareholders are permitted to:

- exercise a liability action against the management of the company when holding 5% of the capital stock represented by shares granting voting rights, limited voting rights, or no voting rights; and
- access information regarding the agenda of any general shareholders' meeting at least 15 days in advance of the day of the meeting.

Management of SABs is entrusted to the board of directors and a chief executive officer (director general). The board of directors may consist of up to 21 members and at least 25% of them must be independent members. See **4.5 Rules/Requirements Concerning Independence of Directors** for more information on independence criteria.

For each proprietary director, an alternate director may be appointed. It is important to note that

alternate directors for independent directors must also meet the independence criteria.

The board of directors of an SAB is supported by the Corporate Practices Committee and the Audit Committee. These must each have three or more members, who must be independent. In SABs controlled by a person or group of people with 50% or more of the capital stock, the Corporate Practices Committee may comprise at least a majority of independent members that will be disclosed to the public.

SABs have no statutory auditor. Monitoring of the company's activities is entrusted to the board of directors, through its Corporate Practices and Audit Committees, and to the external auditor.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

The most recent significant amendment to the General Law of Business Companies was made in October 2023 to incorporate provisions permitting remote meetings of shareholders, partners, directors, or managers. To take advantage of this change, amendments to the by-laws are necessary to expressly allow remote meetings.

In December 2023, amendments to the Securities Market Law were introduced to increase the number of companies with publicly traded shares. These changes allow SABs to issue shares with varying rights and restrictions. This flexibility enables founders or owners of companies to maintain control of the company by offering shares with limited corporate rights when opting to list and offer shares to the public.

Building on these amendments to the Securities Market Law, the National Banking and Securities

Commission (*Comisión Nacional Bancaria y de Valores*) issued the General Provisions applicable to Simplified Issuers (*Disposiciones de Carácter General Aplicables a las Emisoras Simplificadas y los Valores Objeto de Inscripción Simplificada*), which came into effect on 22 January 2025. These provisions establish a tiered framework categorising simplified issuers into: Simplified Equity Issuers (for stocks), Level I Simplified Issuers (for debt instruments with lower thresholds), and Level II Simplified Issuers (for debt instruments and asset-backed securities). The framework also contemplates Structured Securities, though their specific requirements are still not defined. Simplified securities can only be offered to institutional and qualified investors. Simplified disclosure requirements and streamlined registration processes are applicable to simplified issuers compared to traditional ones.

Likewise, and in contrast to private corporations, where authority rests solely with the general shareholders' meeting, SABs and SAPIBs now have the option to delegate authority to their board of directors to increase the capital stock and also determine the terms of the subscription of the shares.

On 30 April 2025, the Mexican Supreme Court's First Chamber issued a ruling (*Amparo directo en revisión 767/2023*) that materially impacts the civil liability framework for directors of Mexican companies.

The ruling confirms that directors can face individual liability in non-contractual matters when shareholders or partners suffer direct personal harm, such as unjustified refusal to register them in the corresponding corporate book or failure to pay dividends to specific shareholders or partners. The Court distinguished this individual action, based on article 1910 of the Federal Civil

Code, from the traditional social action that aims at protecting the company's assets pursuant to Articles 161 and 163 of the General Law of Business Companies.

While this decision significantly strengthens shareholder or partner protection and access to justice, it simultaneously creates new liability risks for individuals serving as directors or board members of Mexican companies.

2.2 ESG Considerations

Mexico has recently strengthened its ESG framework. Following the December 2023 amendment to the Securities Market Law that authorised the Ministry of Finance and Public Credit to issue provisions on sustainable development, the Mexican Council for Financial Information and Sustainability Standards (CINIF) published the Sustainability Information Standards (NIS A-1 and NIS B-1) in 2024. Subsequently, on 28 January 2025, amendments to the General Provisions for Securities Issuers (*Disposiciones de Carácter General Aplicables a las Emisoras de Valores y a otros Participantes del Mercado de Valores*) were published, requiring issuers to prepare and disclose sustainability information following the IFRS Sustainability Disclosure Standards (IFRS S1 and IFRS S2) issued by the International Sustainability Standards Board (ISSB).

The January 2025 amendments require issuers to submit a Sustainability Report that discloses information about sustainability-related risks and opportunities that could reasonably be expected to affect their cash flows, access to financing, or cost of capital in the short, medium, or long term. The report must include information on governance, strategy, risk management, and related metrics and objectives. The obligation to submit these reports begins in 2026 (with

regards to the annual information corresponding to 2025).

Furthermore, on 1 January 2025, an amendment to the General Provisions on Insurance and Bonds (*Circular Modificatoria 2/24 de la Única de Seguros y Fianzas*) came into effect, which requires insurance and bonding institutions in Mexico to incorporate ESG criteria in their investment decisions and asset-management practices. These entities must now include such criteria in their investment policies.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The main bodies involved in the governance and management of a corporation are the shareholders' meeting and the board of directors.

Certain companies may also have committees that aid the company's managing body (eg, Auditing and Corporate Practices Committees). Such committees are mandatory for publicly listed companies, as discussed in **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**.

For private companies, statutory auditors also play an important role in monitoring the activities of the company's management body.

3.2 Decisions Made by Particular Bodies

The general shareholders' meeting is the most important corporate body within a corporation. It may approve and ratify all acts and operations of the company, and its resolutions are carried out by the person specifically appointed for this purpose or, in the absence of such an appointee, by the sole manager or by the board of direc-

tors. See **5.3 Shareholder Meetings** for further information.

The board of directors in a private company usually resolves on the granting of powers of attorney, the approval of the annual report that will be presented to the shareholders' meeting, approval of transactions, and appointment of the company's high-ranking officers.

The board of directors in publicly listed companies must approve, among other matters (and with the prior approval of the appropriate committee) the policies and guidelines for the use of the company's (and its subsidiaries') assets by related parties, transactions with related parties, unusual transactions or transactions exceeding certain thresholds, policies for the granting of any loan, financing or guarantee, accounting policies, engagement of external auditors, and guidelines for internal control and internal audit.

The board of directors does not have the authority to approve any matter that the law reserves for the approval of the shareholders' meeting, such as those reserved for extraordinary meetings that are detailed in **5.3 Shareholder Meetings**.

However, there may be exceptions for publicly listed companies, such as the authority that may be delegated to the board of directors to increase and reduce the SAB's or SAPIB's capital stock.

3.3 Decision-Making Processes

These bodies generally make their decisions at meetings, subject to specific rules.

See **5.3 Shareholder Meetings** for details on the rules applicable to the shareholders' meetings.

Unless a higher percentage is set in the company's by-laws, meetings of boards of directors' are considered legitimate when at least 50% of the board members are present, and resolutions are considered legitimate when approved by majority vote. Unless the by-laws state otherwise, the president of the board has a casting vote in the event of a tie. If allowed by the company's by-laws, the members of the board of directors may approve decisions outside of a meeting, if their resolutions are unanimous and confirmed in writing.

4. Directors and Officers

4.1 Board Structure

The board of directors is comprised of two or more members appointed by the shareholders' meeting, and will include at least a chair from this managing body.

The General Law of Business Companies does not set forth a maximum number of members for the board of directors, or any independence requirements. The number of members of the board of directors must be stated in the company's by-laws.

See **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** for details on the board structure of publicly listed companies.

4.2 Roles of Board Members

The board of directors has a chairperson and, in certain cases, a secretary.

Besides having a casting vote, the chair is authorised to represent the board in the execution of acts (if no delegate has been appointed with this purpose).

In publicly listed companies, the chair of the board may suggest the members to be appointed as members of the company's committees, on the understanding that the chair of the board of directors cannot be chairperson of any of the committees.

Private companies are not required to have a board secretary. However, a secretary (who may or may not be a member of the board) is usually appointed, and is in charge of keeping corporate records and issuing certificates on shareholding structure or other corporate information.

In an SAPIB, the secretary of the board of directors must certify the company's shareholding structure if the company would like its shares registered on the stock exchange.

In an SAB, the board of directors must appoint a secretary who is not a member of the board of directors but who must comply with most of the obligations and duties applicable to the members of the board. The secretary must review and confirm that the shareholders are duly represented at shareholders' meetings, and must certify the authenticity or truthfulness of certain corporate documents that must be filed before the securities authorities.

4.3 Board Composition Requirements/Recommendations

Even when there are no specific requirements for the composition of a private company's board of directors, the Code for Best Corporate Governance Practices issued by the Mexican Business Council (*Consejo Coordinador Empresarial*) updated as of February 2025, recommends appointing no less than three and no more than fifteen members.

In addition, for private companies, the Code suggests that:

- the board includes committees that aid the board in making decisions on auditing; evaluation and compensation; finance and planning; and risk and compliance;
- an uneven number of board members be maintained;
- no alternate members be appointed but, if necessary, the principal member should participate in the selection process of its corresponding alternate;
- at least 25% of the members of the board be independent;
- for the roles of general director and president of the board of directors different individuals be appointed;
- the independent member(s) provide a statement regarding their compliance with independence requirements and reveal potential conflicts of interests;
- at least every four years, an independent consultant prepares a performance assessment of the board and of each board member individually;
- the company sets forth guidelines for the retention and succession of board members, with special focus on independents; and
- women be included.

4.4 Appointment and Removal of Directors/Officers

Those who are legally disqualified from engaging in commercial activities may not serve as members of the board. Additionally, for publicly listed companies, no person who has held the position of external auditor of the company (or any of the entities of its corporate group) during the 12 months immediately preceding the date of appointment can be appointed as a member of the board of directors.

Members of the board of directors are appointed and removed by the general shareholders' meeting. In publicly listed companies, the board of directors must approve the election, appointment, and removal of the chief executive officer and their compensation. Approval by the board is also required for the guidelines for appointing and compensating other high-ranking officers.

4.5 Rules/Requirements Concerning Independence of Directors

Independence

There is no mandatory independence requirement for the members of the board of private companies. In publicly listed companies, at least 25% of the members of the board must be independent.

The independent directors and, if applicable, their respective alternates, should be chosen based on their experience, capacity, and professional reputation. They must fulfil their duties without conflicts of interest and without being influenced by personal, financial, or economic factors. The independence of directors will be evaluated by the general shareholders' meeting during their appointment or ratification.

The following individuals do not qualify as independent.

- High-ranking officers or employees of the company (or any entity of the company's corporate group), as well as their statutory auditors, who have held these positions within the past 12 months.
- Individuals with significant influence or control over the company (or any entity within the company's corporate group).
- Shareholders who are part of the controlling group of the company.

- Customers, service providers, suppliers, debtors, creditors, partners, directors, or employees of entities that have significant business relationships with the company. A business relationship is considered significant if the company's sales to or purchases from the entity account for more than 10% of the entity's total sales or purchases during the prior 12 months or if a loan amount is greater than 15% of the assets of the company or its counter-party.
- Individuals related by blood, marriage, or civil union up to the fourth degree, as well as spouses or partners of the individuals referred to in the preceding paragraphs.

Conflicts of Interest

If a member of the board of directors has a conflict of interest with respect to a particular transaction, they are required to disclose this to the other directors and abstain from voting on the matter. Any director found to violate this provision will be held liable for any damage or losses incurred by the company.

The Code suggests that, upon acceptance of the appointment as board member, each individual submits a statement to the Company disclosing potential conflicts of interest. Additionally, it is suggested that the board member with the conflict of interest be excused from board meetings while the matters in question are discussed.

The same principle applies for publicly listed companies. According to the Securities Market Law, board members (and the secretary) are prohibited from participating in the discussion of such matters, and their absence shall not affect the required quorum for the board to be considered legally convened. Breaching this rule and failure to disclose the conflict of interest is

considered a violation of the director's duty of loyalty.

Internal control and/or auditing committees are typically in charge of overseeing matters related to conflicts of interest, paying special attention to transactions with related parties.

As a good practice, the Code recommends that companies have structures in place to provide anonymous tips regarding conflicts of interests.

4.6 Legal Duties of Directors/Officers

Directors and officers are required to act according to the company's by-laws and all relevant laws and regulations. The duties of officers may also be outlined in an agreement.

Directors are obliged to maintain confidentiality regarding any matters or information to which they gain access in the course of their duties. However, exceptions to this rule exist when such information is requested by judicial or administrative authorities. This confidentiality obligation is valid throughout their tenure and for one year afterwards.

Furthermore, members of the board of directors are jointly liable for the following:

- shareholders' contributions;
- adhering to all requirements for the distribution of dividends;
- establishing and maintaining accounting, control, recording, filing, and information systems, as mandated by law; and
- faithfully executing the resolutions adopted by the shareholders' meeting.

Additionally, directors are jointly and severally liable with their predecessors for any known mis-

conduct that they do not report in writing to the statutory auditor.

In publicly listed companies, the members of the board of directors are also expressly bound by the duty of care and the duty of loyalty.

Under the duty of care, the members of the board of directors are required to perform their duties diligently, in good faith, and in the best interests of the company. Members of the board of directors are considered to have breached their duty of care when they:

- refrain from attending meetings of the board of directors, and any committees to which they belong, and their absence prevents the body from legally convening, unless by justified cause as determined by the shareholders' meeting;
- withhold relevant information necessary for proper decision-making by the board or committees, unless legally or contractually obligated to maintain confidentiality; or
- fail to fulfil their obligations set forth in the company's by-laws or the applicable law.

Members of the board of directors breach their duty of loyalty when, among other examples, they:

- obtain financial gains for themselves or facilitate them for third parties, including specific shareholders or shareholder groups without legitimate cause and due to their position;
- vote in the board of directors' meetings with a conflict of interest;
- do not disclose conflicts of interest;
- intentionally favour a specific shareholder or group of shareholders within the company to the detriment or prejudice of the other shareholders;

- misuse relevant information that is not public knowledge; and
- take advantage of or exploit, for their own benefit or in favour of third parties, without the corresponding waiver of the board of directors, business opportunities that relate to the company or legal entities that are controlled by the company, or in which the company has significant influence.

4.7 Responsibility/Accountability of Directors

Directors owe their duties to the company, and, in the case of publicly listed companies, the legal entity controlled by the company or in which the company has significant influence. That is why any liability action, under the General Law of Business Companies or the Securities Market Law, is considered to be exclusively in favour of such entities, regardless of the person or group that initiates it.

In publicly listed companies, members of the board of directors are not individually or jointly liable for damages or losses incurred by the corporation (or entities controlled by the company, or in which the company has significant influence), provided they act in good faith and meet various conditions, which include the following:

- they comply with the requirements established by law or the company's by-laws;
- they base their decisions or votes on information provided by high-ranking officers, the external auditor, or independent experts, whose capacity and credibility do not raise any reasonable doubt;
- they base their decisions on the most appropriate alternatives available at the time, to the best of their knowledge and belief, or where adverse consequences could not be foreseen considering the information available; and

- they adhere to the resolutions of the shareholders' meeting, provided such resolutions do not violate the law.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Under the General Law of Business Companies or the Securities Market Law, as applicable, the liability of directors may only be demanded by a resolution of the general shareholders' meeting. Directors who have been removed due to alleged liability can only be reinstated if the judicial authority deems the action against them to be unfounded. Upon the resolution by the general shareholders' meeting demanding their liability, directors will cease to perform their duties.

See **5.4 Shareholder Claims** for information on requirements to initiate a liability action for private and publicly listed companies.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

The liability of board members of publicly traded companies for damages caused due to their lack of diligence shall be joint and several among those responsible for the decision or for preventing the board from legally convening.

This liability may be limited, as specified in the by-laws or by resolution of the general shareholders' meeting, provided the actions in question are not fraudulent, in bad faith, or unlawful. Stock corporations may provide indemnifications and insurance coverage for board members, except in cases of fraudulent, bad faith, or unlawful acts.

Corporations and SAPIs are also permitted to expressly set forth in their by-laws limitations to the liability of the members of the board of directors or other high-ranking officers, provided

that such acts are not fraudulent, in bad faith, or unlawful.

A recent ruling by the Mexican Supreme Court has changed the framework concerning directors' civil liability in Mexico and confirmed that there is a pathway for individual actions, under civil law. See **2.1 Hot Topics in Corporate Governance** for more information.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Remuneration of the members of the board of directors may be determined in the company's by-laws. In their absence, the ordinary shareholders' meeting shall determine such remuneration.

In publicly listed companies, the board of directors must approve the remuneration for the chief executive officer and the guidelines for appointing and compensating other high-ranking officers.

Members of the board of directors shall receive no payment that may be considered to breach their duty of loyalty or any other of their duties.

4.11 Disclosure of Payments to Directors/Officers

Private companies are not required to disclose the compensation or any other amount paid to their directors or officers.

For public disclosure, publicly listed companies shall deliver to the National Banking and Securities Commission and the corresponding stock exchange, periodic reports, including information concerning the chief executive officer's compensation and guidelines for appointing and compensating high-ranking officials.

Public listed companies' annual reports that are disclosed to the public provide information on the aggregate compensation paid to the board of directors and other high-ranking officers of the company.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The shareholders are the owners of the company. The relationship between the shareholders and the company is governed by law, the provisions of the company's by-laws, and, if applicable, by any shareholders' agreement.

While transparency requirements related to shareholding structure have increased in recent years, there is no fully public, universally accessible registry of all company shareholders. Certain information about shareholders of publicly listed companies is more accessible due to disclosure requirements under securities regulations. See **5.5 Disclosure by Shareholders in Publicly Traded Companies** for more information.

5.2 Role of Shareholders in Company Management

Shareholders are not required to participate in the company's management. Directors may or may not be shareholders. If the shareholders are not members of the board of directors, they may not be able to direct the management of the company unless they have the right to appoint a member of such a body.

Besides appointing a member of the managing body, shareholders may have an impact or influence on the actions of the business by exercising the corporate rights that they are entitled to depending on the percentage of shares

held, such as calling meetings, delaying votes, or exercising a liability action against the company's management.

5.3 Shareholder Meetings

The general shareholders' meeting is the most important corporate body of a corporation. It may approve and ratify all acts and operations of the company, and its resolutions are carried out by the person specifically appointed for such purposes or, where there is no designation, by the sole manager or the board of directors.

Meetings must be held in the company's corporate domicile, which is a territory (usually a city) indicated in the by-laws. They can take place remotely if the by-laws allow.

The by-laws may also allow the adoption of resolutions outside a meeting if approved by a unanimous vote of the shareholders representing all the voting shares, provided that they are confirmed in writing.

Shareholders' meetings of corporations are divided into ordinary and extraordinary meetings. Ordinary meetings solve any matter not reserved for an extraordinary meeting. While an ordinary meeting can be convened at any time, the law mandates that such a meeting must be held at least once a year, within the first four months of each calendar year, to address any matter of the agenda in addition to: (i) approving the annual report of the managing body; (ii) appointing or ratifying the appointment of the members of the managing and surveillance bodies; (iii) if applicable, approving the compensation of directors and statutory auditors.

Extraordinary meetings are held whenever required to resolve any of the following matters of the corporation:

- extension of duration;
- early dissolution;
- increase or reduction of capital stock (changes to the variable portion of the capital are usually approved in an ordinary meeting);
- change of corporate purpose;
- change of nationality;
- transformation;
- mergers;
- issuance of preferred shares;
- redemption by the corporation of its shares and issuance of beneficial shares (*acciones de goce*);
- issuance of bonds;
- any other amendment to the by-laws; and
- any other matters for which the law or the by-laws require a special quorum.

A corporation's ordinary meeting is deemed to be legally convened when at least half of the capital stock is represented in the meeting, and its resolutions are deemed valid when adopted by the majority of the votes present. In contrast, an extraordinary meeting is legally convened when at least 75% of the capital stock is represented, and its resolutions are valid when approved by shareholders at the meeting representing at least half of the capital stock.

If it is not possible to convene the meeting on the date it was called (usually for lack of quorum), a second meeting will be called and the items on the agenda resolved irrespective of the number of shares represented on the understanding that extraordinary meetings always need to be approved by shareholders at the meeting representing at least half of the capital stock to approve an item.

Companies' by-laws may set higher percentages for either type of meeting to be deemed legally convened and to adopt resolutions.

Shareholders may be represented in the general shareholders' meetings by attorneys-in-fact. Such representation shall be conferred upon on the terms outlined in the by-laws or, where there is no provision, in writing. This special power of attorney is usually granted through a proxy letter (*carta poder*). Directors and statutory auditors are not permitted to represent shareholders in a shareholders' meeting.

If a corporation has multiple categories of shareholders, any proposal potentially affecting the rights of a specific category must first be approved by that affected category convened in a special meeting. Resolution by the special meeting requires the same majority that is required for the amendments of the by-laws of the corresponding company, and must consider the total number of shares within the affected category.

Special meetings must adhere to most of the rules applicable to general meetings, such as the meeting being held at the corporate domicile (or remote attendance if allowed by the by-laws), procedures for calling the meeting, and representation of shareholders, among other requirements.

5.4 Shareholder Claims

Under the General Law of Business Companies, shareholders representing at least 25% of the capital stock are entitled to bring a liability action against board members, provided certain requirements are met. Firstly, the claim must encompass the total amount of liabilities in favour of the corporation, rather than solely representing the personal interests of the plaintiffs. Additionally, if applicable, the plaintiffs must not have voted in favour of the resolution adopted by the general shareholders' meeting that bars them from proceeding against the defendant

directors. Any assets obtained because of these actions will be received by the corporation.

Under the Securities Market Law, liability actions in a publicly listed company may be initiated by the SAB or by the SAB's shareholders that hold at least 5% of the capital stock represented by shares granting full voting rights, limited voting rights, or that have no voting rights. In this case, the action will only favour an SAB or, in certain cases, the company controlled by the SAB or in which the SAB has a significant influence, that suffers property damage.

The ordinary statute of limitations in commercial matters is ten years. However, the statute of limitations is five years for any actions derived from the by-laws and any corporate transactions in connection with any rights and obligations between the corporation and the shareholders (including any action among shareholders). The Securities Market Law expressly sets forth that an action for which accountability from the members of the board of directors is sought will be subject to a five-year statute of limitations, starting on the day on which the act or event causing the corresponding property damage occurred.

The Mexican Supreme Court's First Chamber recently confirmed that, under civil law, shareholders and partners may initiate individual actions against directors for acts or omissions that cause direct personal harm without the need to show damage to the company or comply with the requirements of other social actions, such as those set forth in the General Law of Business Companies. Please refer to **2.1 Hot Topics in Corporate Governance** for further information.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Certain acquisitions of publicly listed securities trigger a disclosure obligation. A person or group of people who acquire, directly or indirectly, in one or several simultaneous or successive transactions of any nature, the common shares of a publicly listed company, resulting in a shareholding equal to or greater than 10% and less than 30% of such shares, will be obliged to disclose such circumstance.

If the acquisition was carried out by a group of people, they must disclose the individual holdings of each of the members of the group. Likewise, the acquirers must disclose whether they intend to acquire significant influence in the company.

If any related party (as defined by the Securities Market Law) of the publicly listed company increases or reduces its ownership stake in the company's capital stock by 5%, whether directly or indirectly, in one or several simultaneous or successive transactions of any nature, it must disclose such information to the public.

Furthermore, any person or group of people who directly or indirectly hold 10% or more of the shares representing the capital stock of publicly listed companies, as well as the members of the board of directors and relevant officers of such companies, must inform the National Banking and Securities Commission and, in certain cases, disclose to the public the acquisitions or transfers of such securities.

Likewise, shareholders are required to inform the publicly listed company of the execution of any shareholders' agreement so that the company can disclose it to the public. These agreements are not binding on the company, and their vio-

lation does not invalidate votes at shareholders' meetings. However, they are enforceable between the parties only after public disclosure.

Publicly listed companies are obligated to submit a report upon the initial registration of their securities and annually thereafter detailing the name and shareholding of several parties, including the companies and individuals that are beneficiaries, whether directly or indirectly, of 5% or more of the company's capital stock.

Disclosure must be made through the relevant stock exchange and under the terms and conditions established by such stock exchange.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Companies must hold an annual general shareholders' meeting that must review and, if applicable, approve the following:

- a report by the board of managers on the company's performance during the preceding fiscal year, the policies followed by the directors, and the main existing projects, if any;
- a report stating and explaining the main accounting and information policies and criteria followed in the preparation of financial information;
- the company's annual financial statements; and
- a report prepared by the statutory auditor on the truthfulness and adequacy of the information submitted by the board of directors.

Failure to submit the annual report on a timely basis will be grounds for the general shareholders' meeting to remove the sole manager or the

members of the board of directors or the statutory auditors without prejudice to any action against them for any liabilities they may have incurred.

Within the 15 days following the date of the annual general shareholders' meeting, the shareholders may request that the financial statements be published on the electronic platform of the Ministry of the Economy. This is not a mandatory, and it is not customary.

Publicly listed companies must disclose periodic financial and accounting information set down mainly in the Securities Market Law and the General Provisions for Securities Issuers, based on the requirements and instructions stipulated therein. Among other things, this includes the submission of an annual report signed by the chief executive officer, as well as officers from the legal and financial departments of the company, and the external auditor. As discussed in **2.1 Hot Topics in Corporate Governance**, simplified issuers are required to disclose information, as provided for in the General Provisions applicable to Simplified Issuers.

6.2 Disclosure of Corporate Governance Arrangements

There is no legal requirement for private companies to disclose their corporate governance arrangements.

However, disclosure requirements for publicly listed companies include the following:

- continuous reports regarding corporate acts, resolutions adopted by corporate bodies and notices that must be given in compliance with the corresponding by-laws or other applicable provisions;

- reports on corporate restructurings such as mergers, spin-offs, acquisitions, or asset sales approved by the shareholders' meeting or the board of directors of the company; and
- shareholders' agreements.

6.3 Companies Registry Filings

Except for simplified corporations, business corporations are set up before a public notary. Companies' incorporation deeds must be registered before the Public Registry of Commerce. Any person who acts on behalf of the company before the corresponding registry is made will be joint and severally liable for any act carried out.

The Public Registry of Commerce maintains records for all registered companies, allowing the public to obtain copies that provide certain information on registered acts. However, copies of the actual registered documents are not publicly accessible. The provided information typically includes details such as changes in corporate name, registered corporate domicile, fixed capital amount, and granted powers of attorney, among others. However, it does not include the current shareholding structure of the company.

The Public Registry of Commerce is aimed at providing publicity regarding certain legal acts that must be registered to be effective against third parties. Unlike other Mexican authorities, it does not have surveillance powers.

Companies that have foreign shareholders must be registered before the National Registry of Foreign Investments (*Registro Nacional de Inversiones Extranjeras*).

Registered companies are required to do the following.

- Renew their registration annually by submitting a form containing their financial information. This requirement applies only if, at any point during the fiscal year, the company's total assets, liabilities, income, or expenses exceed MXN110 million (approximately USD6.5 million, using an exchange rate of MXN17 for USD1).
- File quarterly notices in the event of: (i) amendments to their corporate information; and (ii) changes in certain accounts exceeding MXN20 million (approximately USD1.2 million, using an exchange rate of MXN17 for USD1). These accounts include accounts receivable from or payable to foreign entities within the same corporate group, contributions from the holding entity, capital reserves, or results brought forward from previous years.

The threshold amounts that trigger the obligation to file periodic notices before the National Registry of Foreign Investments are subject to updates or modifications by the authority.

Companies failing to make the necessary filings before the National Registry of Foreign Investments will be subject to fines. No public information is available in connection with these filings.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Closely held companies are not required to appoint an external auditor. However, this appointment is mandatory for publicly listed companies since the external auditor plays a significant role in reviewing the company's financial information, which is periodically disclosed to the public.

The key requirements governing the relationship between the publicly listed company and the auditor are outlined in the Securities Market Law.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

There are no express provisions about the management of risk and internal controls for private companies.

In publicly listed companies, the board of directors must approve the internal control and internal audit guidelines and must follow up (whether directly or via the Audit Committee) on the company's main risks, identified based on the information presented by the committees, the chief executive officer, and the external auditor, as well as the accounting, internal control, and internal audit, registration, filing or information systems.

The audit committee of public companies is also obliged to inform the board of directors of the status of the internal control and internal audit system and any irregularities detected.

Publicly listed companies must disclose, annually and quarterly, any amendments made with respect to internal controls and audit. Such changes must have been previously approved by the board of directors and have been approved by the Audit Committee.

NETHERLANDS



Law and Practice

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Stibbe is a leading independent international law firm with main offices in Amsterdam, Brussels and Luxembourg, and a branch office in London. The firm provides the highest-quality service in legal advice, transactions and litigation. The dedicated multidisciplinary teams are trusted legal advisers to clients, which range from national and multinational companies and financial institutions to government organisations and other public authorities. **Stibbe** han-

dles transactions, disputes and projects across a wide range of sectors. The firm's understanding of clients' commercial objectives enables it to provide suitable and effective advice on complex legal issues and challenges. It works closely with other international top-tier firms on cross-border matters outside its home jurisdictions; the firm's independence allows it to team up with any foreign law firm to suit clients' needs and preferences.

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The Stibbe logo, featuring the word "Stibbe" in a large, dark blue, serif typeface, centered within a light gray rectangular background.

1. Introductory

1.1 Forms of Corporate/Business Organisations

The BV and the NV

Under Dutch law, the principal forms of corporate and business organisations are categorised into legal entities with legal personality and entities without legal personality. The corporate entities that are frequently used for commercial activities in the Netherlands are:

- the private company with limited liability (*besloten vennootschap met beperkte aansprakelijkheid* or BV); and
- the public company with limited liability (*naamloze vennootschap* or NV).

The BV and the NV are legal persons under Dutch law. Their equity is divided into shares that are held by one or more shareholders.

The BV is the most frequently used type of corporate entity in the Netherlands. In 2024, 1,156,074 BVs and 3,133 NVs were registered in the Netherlands. Most Dutch listed companies are NVs, but it is also possible to list a BV.

The definition of “Dutch listed company” in this chapter refers to (i) all companies with registered offices in the Netherlands whose shares or depositary receipts for shares have been admitted to trading on a regulated market or a comparable system; and (ii) all large companies with registered offices in the Netherlands (balance sheet value > EUR500 million) whose shares or depositary receipts for shares have been admitted to trading on a multilateral trading facility or a comparable system).

Other Entities With Legal Personality

The following legal entities also have legal personality in the Netherlands:

- an association (*vereniging*);
- a co-operative (*coöperatie*);
- a mutual insurance association (*onderlinge waarborgmaatschappij*); and
- a foundation (*stichting*).

Book 2 of the Dutch Civil Code applies to all the legal entities listed in the foregoing.

Entities Without Legal Personality

Entities without legal personality do not constitute separate legal persons but may still operate as business organisations. These include:

- a general partnership (*vennootschap onder firma* or VOF);
- a limited partnership (*commanditaire vennootschap* or CV);
- a professional partnership (*maatschap*); and
- a sole trader (*eenmanszaak*).

These forms are mainly governed by Book 7A of the Dutch Civil Code and the Dutch Commercial Code (*Wetboek van Koophandel*).

Unless otherwise stated, the answers in this chapter will focus on BVs and NVs as the principal corporate forms under Dutch Law.

1.2 Sources of Corporate Governance Requirements

General

Several acts are sources of corporate governance requirements for BVs and NVs. The Netherlands is a member of the EU, which means that Dutch corporate law is based in large part on European regulations, which have been implemented in several relevant Dutch acts.

Dutch Civil Code (*Burgerlijk Wetboek*)

Book 2 of the Dutch Civil Code is the primary source of corporate law in the Netherlands. The following matters are governed by Book 2 of the Dutch Civil Code, among other things:

- the various corporate bodies within a company (eg, general meeting, management board and supervisory board);
- the duties, powers and liabilities of these corporate bodies;
- specific rules on representation and directors' conflicts of interest;
- shareholder rights, including information, meeting and voting rights; and
- financial reporting and disclosure.

Book 2 of the Dutch Civil Code sets out the mandatory and default rules for the governance of legal persons in the Netherlands, and applies to both privately held and publicly listed companies, with some provisions tailored to listed NVs and BVs.

Financial Supervision Act (*Wet op het financieel toezicht*)

In addition, Chapter 5 of the Financial Supervision Act provides for rules on the supervision of the business conduct of a legal entity whose securities are admitted to trading on a regulated market (hereafter, the “*issuing institution*”). It contains rules on the disclosure of major holdings, financial reporting, the prevention of market abuse and the obligations of institutional investors. The Dutch Authority for the Financial Markets (*Autoriteit Financiële Markten* – AFM) supervises compliance with these rules.

Dutch Corporate Governance Code

The Dutch Corporate Governance Code (hereafter, the “*CG Code*”) is a principle-based instrument that applies on a comply-or-explain basis.

The CG Code focuses on the governance of Dutch listed companies and provides guidelines for effective co-operation and management. The CG Code was first established in 2003 and was amended in 2008, 2016 and 2022. The CG Code 2022 came into force on 1 January 2023. Dutch listed companies reported on the CG Code 2022 for the first time in 2024 in the management report for financial year 2023. The Monitoring Committee CG Code (hereafter, the “*Commission*”) issued an update of the CG Code on 20 March 2025, mainly introducing the risk management statement – a new risk management statement that strengthens reporting obligations on risk oversight. See **2.1 Hot Topics in Corporate Governance** for more information on the risk management statement.

The CG Code applies to Dutch listed companies. The purpose of the CG Code, as set out therein, is to realise, with or in relation to legislation and regulations, a sound and transparent system of checks and balances within Dutch listed companies and to regulate the relationships between the management board, the supervisory board and the general meeting/shareholders for this purpose. Compliance with the CG Code should contribute to confidence in good and responsible management of companies and their embedding in society.

The CG Code contains principles and best practice provisions regulating the relationship between the management board, the supervisory board (or the one-tier board as the case may be) and the general meeting/shareholders of Dutch listed companies. The principles and best practice provisions aim to define responsibilities for sustainable long-term value creation, risk control, effective management and supervision, remuneration and the relationship with

shareholders (including the general meeting of shareholders) and stakeholders.

The broad outline of the company's corporate governance is set out each year in a separate chapter of the management report or on the corporate website. Here, the company explicitly states the extent to which it complies with the principles and best practice provisions stipulated in the CG Code and, where it does not comply, why and to what extent it departs from them (comply-or-explain principle).

Articles of Association

The articles of association of a BV/NV may also provide for specific corporate governance provisions within the boundaries of Book 2 of the Dutch Civil Code. They may require, for example:

- a specific quorum or qualified majority resolution for certain resolutions of the general meeting, the supervisory board or the management board;
- the allocation of powers among corporate bodies;
- certain procedures for convening and conducting general meetings; and
- certain procedures for the appointment and dismissal of board members.

The articles of association form a binding framework and play an important role in tailoring the corporate governance of a company.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

General

In addition to the applicable provisions of Book 2 of the Dutch Civil Code, which also contain various specific rules for Dutch listed companies, the following regulations apply to Dutch

listed companies. The requirements of the Acts are mandatory: the requirements (principles and best practice provisions) of the CG Code are based on the “*comply-or-explain*” principle.

Financial Supervision Act (Wet op het financieel toezicht)

See 1.2 Sources of Corporate Governance Requirements.

CG Code

See 1.2 Sources of Corporate Governance Requirements.

Sector-Specific Legislation

Sector-specific legislation is in place for certain entities, such as financial institutions. The healthcare sector, for example, has a Healthcare Governance Code.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In December 2019, the European Commission introduced the European Green Deal, the purpose of which is to transform the EU into a modern, resource-efficient and competitive economy. Several legislative initiatives have since been adopted, including the Corporate Sustainability Reporting Directive (CSRD) and the Corporate Sustainability Due Diligence Directive (CSDDD).

CSRD

The CSRD imposes an obligation for a large group of companies to report on their sustainability efforts in line with the European Sustainability Reporting Standards (ESRS). This Directive came into force on 5 January 2023 and should have been implemented by member states by July 2024. However, several member states, including the Netherlands, have missed

this deadline. On 13 January 2025, a bill for the CSRD implementation was submitted to the Dutch Lower House.

CSDDD

On 23 February 2022, the European Commission published the proposal for the CSDDD, which aims to harmonise existing EU member state laws on supply chain due diligence, obligations regarding actual and potential human rights adverse impacts and environmental adverse impacts with respect to their own operations and those of their subsidiaries and other entities in their value chain. The directive entered into force on 25 July 2024 and must be implemented by member states by July 2026. On 18 November 2024, a draft bill to implement the CSDDD in the Netherlands was published for consultation.

Omnibus Packages

On 26 February 2025, the European Commission adopted a package of proposals in the form of two omnibus packages aimed at simplifying ESG regulations in the EU, whilst boosting competitiveness. These proposals include amendments to the CSRD and CSDDD to reduce regulatory burdens and give companies additional time to prepare for compliance. On 3 April 2025, the European Parliament, having used a fast-track procedure, voted to approve the directive that included those amendments and postponed reporting and due diligence obligations under the CSRD and CSDDD. This “*stop-the-clock*” directive entered into force on 17 April 2025. See **2.2 Environmental, Social and Governance (ESG) Considerations** for more information on the proposed amendments to the CSRD and CSDDD in the omnibus packages.

CG Code

The main theme of the CG Code 2022 is sustainable long-term value creation. On 20 March 2025,

the CG Code was updated. This update relates in particular to the risk management statement (*Verklaring Omtrent Risicobeheersing*). Under the updated CG Code, the management board of a company must declare the following in its management report. First, that internal risk management and control systems provide at least a limited level of assurance. Second, that the sustainability reporting does not contain any material misstatements. Third, the level of assurance these systems provide that the operational and compliance risks are controlled effectively. The risk management statement serves to provide transparency to stakeholders on the management of operational, compliance and reporting risks. See **1.2 Sources of Corporate Governance Requirements** for more information on the CG Code.

Milieudefensie/Shell

See **4.7 Responsibility/Accountability of Directors** for further information regarding these cases.

Milieudefensie/ING

On 28 March 2025, Dutch environmental group Milieudefensie, filed a lawsuit against ING, alleging that the bank failed to meet its climate obligations (ie, to cut its total emissions in half and stop working with companies with high pollution levels). The lawsuit demands that ING halves its total emissions by 2030 compared to 2019 levels and implements stricter climate policies across eight high-pollution sectors, including steel and aviation. Milieudefensie, also calls for ING to stop financing companies involved in new oil and gas projects and to require all large corporate clients to submit credible climate transition plans. The NGO argues that ING’s current approach is insufficient in addressing its climate impact, despite the bank’s claims of prioritising

sustainability. The Amsterdam District Court has not yet issued a ruling.

2.2 ESG Considerations

The CSRD requires companies to publish reports on the policies, targets, performance, impacts, risks and opportunities in relation to ESG aspects of the company. The CSRD revises and strengthens rules introduced by the Non-Financial Reporting Directive (NFRD). It aims to ensure that companies provide reliable, consistent and comparable sustainability information for investors and other stakeholders.

Reporting must be done in accordance with the ESRS adopted by the European Commission. The CSRD requires companies to publish their sustainability reports in a dedicated section of their annual management reports.

Taking into account the postponements introduced by the “*stop-the-clock*” directive, the CSRD applies to financial years starting on or after:

- 1 January 2024 for large Dutch I listed companies that already have to report in order to conform with the NFRD;
- 1 January 2027 for large companies (*grote vennootschappen*); and
- 1 January 2028 for listed SMEs, which will be subject to a mitigated reporting regime.

The CSRD requires an independent assurance services provider to provide an assurance opinion on sustainability reporting. Initially, during the first few years of application of the CSRD, this opinion may be based on a limited assurance engagement. In the future, however, this may be extended to a reasonable assurance engagement after an assessment by the European Commission of the feasibility of such extension.

However, in the omnibus package, it is proposed that this possibility for the European Commission to propose moving from a limited assurance requirement to a reasonable assurance requirement be removed.

CSDDD

The CSDDD sets out to ensure that large companies operating in or trading with the EU integrate environmental and human rights due diligence into their corporate governance. Its scope targets EU companies with over 1,000 employees and a global turnover of more than EUR450 million. Non-EU companies generating at least EUR450 million within the EU also fall under the scope of the CSDDD.

The CSDDD mandates that in-scope companies adopt effective due diligence policies to identify, prevent or mitigate – and ultimately end – any adverse impact of their operations on human rights, the environment and good corporate governance (including corruption).

Key obligations include:

- implementing “*appropriate measures*” across the entire value chain;
- expanding the scope of adverse impacts to cover a broader range of human rights issues; and
- developing a strategic plan to align business models with the global target of limiting warming to 1.5°C.

Omnibus Packages

On 26 February 2025, the European Commission published two omnibus simplification packages, introducing proposals to reduce sustainability requirements following from EU legislation.

The first omnibus package contains a proposal with temporal changes that postpone the application of all reporting requirements in the CSRD for companies that are due to report in 2026 and 2027 (so-called wave 2 and 3 companies, respectively) and postpone the transposition deadline and the first wave of application of the CSDDD by one year to 2028. This directive entered into force on 17 April 2025.

Further, this omnibus package includes a proposal with substantive changes, such as raising the employee threshold for mandatory sustainability reporting under the CSRD from 250 or more to 1,000 employees. If adopted, this change would significantly reduce the number of companies required to report, exempting approximately 85% of businesses that currently fall under the directive. Listed SMEs, which were previously required to report under the CSRD, would also be removed from the scope. Under the new threshold, only companies with at least 1,000 employees and either a turnover above EUR50 million or a balance sheet total exceeding EUR25 million would be subject to reporting obligations.

The Commission has outlined an explicit goal of reducing reporting burdens by 25% for large companies and 35% for SMEs, reflecting a broader effort to simplify sustainability disclosures while maintaining the EU's ambitious environmental objectives.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

Principal Bodies of BVs and NVs

All BVs and NVs have a management board and a general meeting. BVs and NVs may opt for a

supervisory board or for non-executives in the board, resulting in the following three possible governance structures:

- only a management board is in place, with executive directors;
- both a management board and a supervisory board are in place (a two-tier structure); or
- a one-tier management board is in place, consisting of executive directors and non-executive directors (one-tier board structure).

Large Company Regime (*Structuurregime*)

A supervisory board (or a one-tier board consisting of executive and non-executive directors) is mandatory if a company has filed a statement with the Dutch Trade Register for three consecutive years, stating that it qualifies as “*large*” company under the statutory two-tier rules (*structuurvennootschap*). This supervisory board must consist of three or more directors (or three or more non-executive directors in the case of a one-tier board). Persons employed by the “*large*” company or any of its dependent companies, as well as directors and employees of an employees’ organisation involved in determining the terms of employment of those persons, cannot be appointed as supervisory directors.

See 4.1 **Board Structure** for more information on the one-tier board.

The main characteristics of a company (*structuurvennootschap*) to which the large company regime applies are:

- in principle, the general meeting and the works council (*ondernemingsraad*) can significantly influence the composition of the supervisory board;
- the supervisory board, rather than the general meeting, is authorised to appoint the direc-

tors of the management board and to remove them from office – the supervisory board lacks this authority if the so-called mitigated large company regime applies (as described in the following); and

- certain important resolutions of the management board require the prior approval of the supervisory board (or the majority of the non-executive directors in the case of a one-tier board).

The large company regime (*structuurregime*) is applicable to a Dutch company that has filed a registration with the Dutch Trade Register, stating that from its adopted annual accounts it appears that:

- its issued capital and reserves amount to not less than EUR16 million;
- it has set up a works council on the grounds of a statutory requirement; and
- as a rule, it employs at least 100 employees in the Netherlands.

It must also have kept this mandatory registration with the Dutch Trade Register for three consecutive years. Upon the expiration of this three-year term, the company's articles of association must be amended to incorporate certain mandatory provisions relating to the large company regime.

For the second and third requirements mentioned in the foregoing, the dependent companies (*afhankelijke maatschappijen*) of the company are also taken into account. A company qualifies as a dependent company of another legal entity if, among other things, such other entity provides at least 50% of the capital of such company.

A company that meets the criteria set out in the foregoing is required to file a registration with the Dutch Trade Register within two months after the adoption or approval of the company's annual accounts by the general meeting. A repeated annual registration to fall under the large company regime for consecutive years is not required.

Exemptions

The large company regime does not apply to certain companies, such as:

- companies that exclusively or almost exclusively operate as holding or finance companies for their group companies, provided that the majority of the employees of the group are employed outside the Netherlands; and
- companies of which at least half of the share capital is held by a company that applies the large company regime.

Mitigated Large Company Regime (*Beperkt Structuurregime*)

Certain companies that fall under the large company regime (*structuurvennootschappen*) are allowed to apply the mitigated large company regime (*beperkt structuurregime*) instead of the full large company regime. This applies, for example, to *structuurvennootschappen* in which at least 50% of the share capital is held by a legal entity (either by itself or by its dependent company) that employs the majority of its employees outside the Netherlands. Under the mitigated large company regime, the general meeting appoints the managing directors (as opposed to the supervisory board, which is entitled to appoint the managing directors if the full large company regime applies). For more information, see 4.4 Appointment and removal of Directors/Officers.

Voluntary Application of the (Full or Mitigated) Large Company Regime

A company may also voluntarily apply the provisions of the full or mitigated large company regime if it (or a dependent company) has established a works council to which the provisions of the Works Council Act (*Wet op de Ondernemingsraden*) apply.

3.2 Decisions Made by Particular Bodies

The Management Board

The primary responsibility of the management board is to manage the company and its business. In the performance of its duties, the management board is collectively responsible for:

- formulating and determining the policy and strategy;
- achieving the legal entity's objects; and
- the day-to-day management of the company and its business.

The management board must carry out its duties in line with the company's objectives, which are included in the company's articles of association.

Depending on the articles of association, the management board may resolve on:

- the issuance of shares (if this authority is granted to the management board by the general meeting);
- reservations from the profits;
- (approval of) (interim) distributions; and
- the right of initiative for certain resolutions of the general meeting, such as shares issuances, amendments to the company's articles of association, legal mergers, demergers, dissolution and conversion.

The Supervisory Board

If installed, the supervisory board supervises and advises the management board on the general course of affairs of the company and the business affiliated with it.

General Meeting – Shareholders

In principle, the general meeting may resolve on the following:

- the appointment (including remuneration and, in the case of a one-tier board, designating whether a person is appointed as an executive or non-executive director), suspension and dismissal of managing directors and supervisory directors (see 3.1 **Bodies or Functions Involved in Governance and Management** regarding the deviating provisions applicable to companies subject to the full or mitigated large company regime);
- any increase (including the issuance of shares) or decrease of share capital;
- the adoption of the annual accounts;
- distributions;
- amendments to the company's articles of association, covering legal mergers, demergers, dissolution and conversion; and
- the appointment of the auditor.

The general meeting is entitled to receive information from the management board.

The articles of association may provide that certain management board resolutions are or can be made subject to the approval of the general meeting or supervisory board.

For the NV, the approval of the general meeting is required for resolutions of the management board concerning a major change in the identity or character of the company or business.

Listed Company

General meetings of a Dutch listed company hold an advisory vote on the remuneration report and adopt the remuneration policy for the management board and supervisory board every four years. The resolution to adopt the remuneration policy requires a 75% majority of the votes validly cast, unless the articles of association explicitly provide otherwise.

3.3 Decision-Making Processes

Management Board

The management board has collective responsibility. If collegial governance is in place, it is possible to make a division of tasks. The responsibility for fulfilling a particular board task, as part of the board policy, always remains with the entire board.

Each managing director has one vote. The articles of association may provide that a director has more than one vote, but one director cannot have more votes than the other directors collectively.

Dutch law does not include quorum requirements (the articles of association may provide otherwise). The management board adopts resolutions by simple majority of the votes validly cast (the articles of association may provide otherwise). Meeting and decision-making rules can be included in the articles of association and elaborated on in the regulations of the management board. The management board adopts resolutions inside a meeting; resolutions outside a meeting are allowed, depending on the articles of association.

Supervisory Board

The characteristics of the collective responsibility of the management board and the decision-

making process as described in the foregoing are also applicable to the supervisory board.

Shareholders Meeting

The general meeting of a BV/NV is led by a chair, who is responsible for the meeting order; often, the chair of the supervisory board is the chair of the general meeting.

Every shareholder of a BV/NV has the right to attend the general meeting, speak at it and exercise voting rights, either in person or by written proxy.

A BV may have non-voting shares; shareholders with non-voting shares cannot vote but do have the right to attend the general meeting.

Managing directors and supervisory directors have an advisory vote to the general meeting.

4. Directors and Officers

4.1 Board Structure

Management Board

Dutch corporate law requires each BV and NV to have a management board that is legally responsible for managing the company and its affiliated businesses. In carrying out their duties, the members of the management board must act in the best interests of the company and its business.

Structure of two-tier board

In addition to the management board, it is possible to have a supervisory board in place (two-tier system). Under the two-tier system, the company has both a management board and a supervisory board. The supervisory board is charged with supervising the policy of the management board and the general affairs of the company,

while also providing advice to the management board.

Structure of one-tier board

Alternatively, the company may adopt a one-tier system in which a single board comprises both executive and non-executive directors. The executive directors are responsible for the daily management of the company. The non-executive directors oversee the performance of the executive directors and are entrusted with supervising the general affairs of the company. All directors in a one-tier board collectively share responsibility for the overall direction and management of the company.

Both members of a supervisory board and non-executive directors in a one-tier board must be individuals. A company that falls under the large company regime (*structuurregime*) is obliged to establish either a separate supervisory board or a one-tier board with non-executive directors, as further addressed in **3.1 Bodies or Functions Involved in Governance and Management**.

4.2 Roles of Board Members

Management Board – Collective Responsibility

The management board of a legal entity is charged with the management of the company and its affiliated business. Specific tasks may be expressly attributed or delegated to an individual managing director or pursuant to the articles of association. The management board is collectively responsible for resolutions, even if resolutions are made by individual board directors.

Taking into account the general duties mentioned in the foregoing, the specific details of the management board's role depend on several factors, such as the size and nature of the legal entity's activities. The responsibilities of the

individual board directors of Dutch companies are often set out in charters of the management board.

Chairperson

Neither Book 2 of the Dutch Civil Code nor the CG Code stipulates who appoints the chairperson of the management board or the supervisory board of an NV or BV.

Roles within a one-tier board

If a company has a one-tier board, the task of supervising the executive directors cannot be taken away from non-executive directors. The chairpersonship of the board, making nominations for the appointment of a director and determining the remuneration of executive directors cannot be assigned to (an) executive director(s).

Roles within a supervisory board

The supervisory board has collective responsibility for supervising the performance of the management board. It may also allocate duties among its members, without this relieving them of their collective responsibility. For Dutch listed companies with more than four supervisory directors, the CG Code sets out that the supervisory board should appoint from among its directors:

- an audit committee;
- a remuneration committee; and
- a selection and appointment committee.

One of the directors of the supervisory board must be a financial expert (this is mandatory law; see **4.3 Board Composition Requirements/Recommendations**). The audit committee and the remuneration committee should not be chaired by the chairperson of the supervisory board, nor by a former managing director of the company.

See also 4.6 Legal Duties of Directors/Officers for more information.

4.3 Board Composition Requirements/Recommendations

General Composition Requirements

The following minimum requirements apply to the composition of boards.

- Two-tier structure:
 - (a) a management board with at least one managing director (who may be a legal person or an individual); and
 - (b) if established, a supervisory board with at least one individual member.
- One-tier board: at least one executive director (who may be a legal person or an individual) and one non-executive director (who must be an individual).

The articles of association may restrict who is eligible to be appointed as a director by imposing specific requirements. Such requirements may be set aside by a resolution of the general meeting if at least two-thirds of the votes are cast in favour, representing more than half of the issued share capital.

Dutch Companies Within the Scope of the CG Code

According to the CG Code, each supervisory director and each managing director should have the specific expertise required for the fulfilment of their duties. Each supervisory director should be capable of assessing the broad outline of the overall management. The requirement that the supervisory board has financial expertise is enshrined in law. Pursuant to the Resolution Establishing an Audit Committee (*Besluit Instelling Auditcommissie*), at least one member of the audit committee must have expertise in the preparation and auditing of annual accounts.

This provision has been implemented in Dutch legislation and is applicable to public interest entities (such as listed companies, banks and (certain) insurance companies).

Diversity

Each year, large companies (*grote vennootschappen*) must set appropriate and ambitious gender diversity targets for the management and supervisory boards and senior management. For the purpose of the Diversity Act (*Wet ingroeiquotum en streefcijfers*), a large company (whether listed or not) is a company that meets at least two of the following requirements on two consecutive balance sheet dates:

- the value of the assets exceeds EUR25 million;
- the net turnover for the financial year exceeds EUR50 million; and
- the average number of employees is 250 or higher.

It does not suffice to include only the size of its own assets, net sales and employees: data from group companies that must be included in the consolidation must also be considered in determining whether the thresholds are met.

Gender diversity – supervisory boards of Dutch companies within scope of the CG Code listed on Euronext Amsterdam

Supervisory boards of Dutch companies listed on Euronext Amsterdam (both NVs and BVs) are subject to a diversity quota of at least one-third male and one-third female directors. If the supervisory board does not meet this diversity quota, any appointment that does not balance the distribution is void, leaving the relevant vacancy open. Every listed company must take the diversity quota into account in every appointment or reappointment of a supervisory director.

The same applies to non-executive directors in the case of a one-tier board.

Additional diversity requirements for companies within scope of the CG Code

The management board, the supervisory board and the executive committee (if any) should be composed in such a manner as to ensure a degree of diversity appropriate to the company with regard to expertise, experience, competencies, other personal qualities, sex or gender identity, age, nationality and cultural or other background.

See **4.2 Roles of Board Members** regarding the composition of the committees of the supervisory board of a Dutch listed company.

Additionally, supervisory boards of Dutch listed companies whose shares or depositary receipts are admitted to trading on a regulated market, as referred to in Section 1:1 of the Financial Supervision Act in the Netherlands, are subject to a diversity quota of at least one-third male and one-third female directors. If the supervisory board does not meet this diversity quota, any appointment that does not balance the distribution is void, leaving the relevant vacancy open. The same applies to non-executive directors in the case of a one-tier board.

Reporting requirements on diversity

Large companies within the meaning of the Diversity Act must report on the following in their management report on diversity in the board:

- the current male/female ratio;
- the target ratios;
- the action plan; and
- the objectives achieved.

In addition, pursuant to the Diversity Act, large companies must set more appropriate and ambitious target ratios and draw up an action plan. Every year, the progress with the obligations under the Diversity Act must be reported to the Social and Economic Council (SER), within ten months of the end of the financial year. The basic principle is that what must be reported in the management report must also be reported to the SER. To this end, the SER has developed a diversity portal. Because large companies are required to report via this portal, it is possible to monitor how these companies satisfy their obligations and how they perform relative to others. Dutch listed companies do not have to report on the supervisory board (or on the non-executive directors on the one-tier board) in the management report, because they must already comply with the diversity quota.

Restrictions on the Number of Positions of Directors

Book 2 of the Dutch Civil Code sets a maximum number of supervisory positions that each managing director or supervisory director is allowed to hold at Dutch large companies (*grote vennootschappen*) and Dutch large foundations.

In principle, a managing director may:

- hold a maximum of two positions as a supervisory director of a large company in addition to their management board position; and
- not be the chairperson of a supervisory board or of a one-tier board of a large company.

A supervisory director may hold a total of five supervisory positions in large companies. The position as chairperson of a supervisory board or one-tier board counts twice.

Under the CG Code, the supervisory board's approval is required if a managing director of the company intends to accept a supervisory board membership elsewhere.

4.4 Appointment and Removal of Directors/Officers

Appointment of Directors

General rules for the appointment of managing and supervisory directors of a BV/NV

The first appointment of supervisory directors (if applicable) and of managing directors is included in the notarial deed of incorporation of the NV/BV. After the incorporation of the NV/BV, the general meeting appoints the managing directors and supervisory directors (unless the large company regime applies). See also **3.1 Bodies or Functions Involved in Governance and Management** for more information on the large company regime.

The articles of association may provide that the appointment of a managing director or supervisory director by the general meeting must be based on a binding nomination. In that case, only the nominated person may be appointed as director. The binding nature of the nomination can be removed by a qualified majority resolution of the general meeting.

With respect to supervisory directors, the articles of association may provide that a maximum of one-third of the supervisory directors may be appointed by third parties.

Specific rules for the appointment of managing and supervisory directors of a BV

For a BV, the articles of association may provide that managing directors and supervisory directors are appointed by a meeting of holders of shares of a certain class or type. Nevertheless,

every shareholder with voting rights must still be involved in appointing at least one managing director and at least one supervisory director.

Specific rules for the appointment of directors of a BV/NV subject to the large company regime (structuurregime)

The supervisory board appoints the managing directors (or the non-executive directors appoint the executive directors in the case of a one-tier board) unless the mitigated large company regime applies, in which case the general meeting appoints the managing (or executive) directors.

The general meeting appoints a supervisory director (or the non-executive directors, in the case of a one-tier board) following a special procedure, including a nomination right of the supervisory board (or non-executive directors); such nomination takes into account the (enhanced) right of recommendation of the works council. Supervisory board members are appointed for a maximum term of four years, which can be extended in the articles of association until the day of the first general meeting after such four-year term.

Removal of Directors

Removal of managing directors

Managing directors of a BV/NV may be suspended and dismissed at any time by the person/body authorised to appoint them. The articles of association of a BV may also grant the power of dismissal to another corporate body. The supervisory board may suspend managing directors at any time, unless the articles of association provide otherwise. The managing directors of a mitigated large company regime may be suspended and dismissed only by the supervisory board.

Removal of supervisory directors

Supervisory directors of a BV/NV may be suspended and removed by the person/body authorised to appoint them. A general meeting of a BV that is not authorised to appoint may nevertheless be granted the power of removal and suspension in the articles of association.

Removal of supervisory directors of a company subject to the large company regime (structuurvennootschap)

Each supervisory director may be subject to the following.

- Suspended by the supervisory board.
- Removed by the Enterprise Chamber of the Amsterdam Court of Appeal on account of:
 - (a) neglect of their duties;
 - (b) other serious reasons; or
 - (c) a drastic change in circumstances based on which their continuation as a director of the supervisory board cannot reasonably be required from the company.

A removal by the Enterprise Chamber may take place on the basis of a request submitted by the company, represented for this purpose by the supervisory board, and also by a representative appointed for this purpose by the general meeting or by the works council.

4.5 Rules/Requirements Concerning Independence of Directors

General

The Dutch Civil Code contains no general provisions on the independence of the supervisory board and individual supervisory directors of a BV/NV. However, it is generally accepted that the supervisory board of a BV/NV should, in principle, be sufficiently independent in relation to the company and its stakeholders.

Supervisory Board of Large Companies (Structuurvennootschap)

The supervisory board of a *structuurvennootschap* must be properly composed. The Dutch Civil Code requires that employees of the company or a dependent company, and union representatives, cannot be supervisory directors.

Independence Requirements of a Company within Scope of the CG Code

The composition of the supervisory board safeguards that the members are able to operate independently and critically in relation to one another, the management board and any particular interests involved.

The following applies under the CG Code (best practice provision 2.1.7 through 2.1.9):

- no more than one supervisory board member meets any of the criteria set out in best practice provisions 2.1.8 (i) through (v), pursuant to which such supervisory director is deemed not independent;
- the total number of supervisory board members to whom the criteria referred to in best practice provisions 2.1.8 (i) through (vii) are applicable should account for less than half of the total number of supervisory board members, pursuant to which such supervisory director is deemed not independent;
- for each shareholder, or group of affiliated shareholders, holding directly or indirectly more than 10% of the company's share capital, no more than one supervisory board member may be deemed affiliated with or representing them, as referred to in best practice provisions 2.1.8 (vi) and (vii); and
- the chair of the supervisory board may not be a former managing director of the company and must be independent within the meaning of best practice provision 2.1.8.

Potential Conflicts of Interest

A managing director or supervisory director may not participate in deliberations and decision-making if they have a direct or indirect personal interest that conflicts with the interests of the company. If a managing director or supervisory director nevertheless participates in the deliberations or decision-making, the management board or the supervisory board resolution becomes voidable. Any conflict of interest has an impact on internal decision-making only. This means that directors with a conflict of interest remain authorised to represent the company. There is, however, a liability risk.

Consequences of a conflict of interest of management or supervisory directors

If no management board resolution can be adopted as a result of a conflict of interest, the resolution may be adopted by the supervisory board. If there is no supervisory board, the resolution may be adopted by the general meeting, unless the articles of association provide otherwise. If all the supervisory directors have a conflict of interest, the resolution is adopted by the general meeting, unless the company's articles of association provide otherwise.

Based on case law, a supervisory director has a duty to provide full transparency about possible conflicts of interest, while keeping conflicting interests separate from the interests of the company. A similar provision applies in the event of a conflict of interest of one or more supervisory directors.

Stricter conflict of interest rules apply to Dutch companies within scope of the CG Code

The CG Code stipulates that any form of conflict of interest between the company and the managing directors or supervisory directors must be

prevented, and that adequate measures should be taken to avoid conflicts of interest. Therefore, high standards of transparency and accountability are expected from Dutch listed companies.

4.6 Legal Duties of Directors/Officers

The entire management board of the company is collectively responsible (see 4.2 Roles of Board Members) for the policy, strategy and day-to-day management of the company, which includes:

- the management of the company (subject to any limitations in the company's articles of association);
- keeping proper company books and records;
- preparing financial reports and publishing annual accounts in time;
- exercising management control (managing the company and its business, determining its general policy and co-ordinating its organisation, including that of the group);
- exercising financial control (managing the company's assets, controlling the flow of funds, administering the company's financial condition); and
- exercising control of the company's legal acts (to ensure regulatory compliance and compliance with the company's articles of association, and to fulfil the duty of care towards third parties, by ensuring that the company observes the legal relationships entered into with the third parties).

In the performance of their duties, directors of all boards must be guided by the best interests of the company and the business affiliated with it. This is generally determined primarily by promoting the continued success of this business (*bestendig succes van de onderneming*). The Dutch Supreme Court added that, in discharging their duties, directors should also – partly based on the principle of reasonableness and fairness

– exercise due care with regard to the interests of all those involved in the company and its business, and that this duty of care may require directors, in serving the company’s interests, to ensure that this does not unduly or disproportionately harm the interests of those involved.

Directors should also keep in mind that the legal entity has an independent interest in ensuring that legal and statutory norms, or norms arising in part from reasonableness and fairness, including procedural norms necessary for proper decision-making, have been or are properly observed. This implies taking into account the interests of all the stakeholders, including shareholders, employees, creditors and other relevant stakeholders.

In addition, companies, corporate bodies and directors have a duty to act towards each other and other corporate bodies in accordance with the principles of reasonableness and fairness.

4.7 Responsibility/Accountability of Directors

General

As mentioned in 4.6 Legal Duties of Directors/Officers, according to Dutch corporate law, all management and supervisory directors must act in the interest of the company and the business affiliated with it. The interest of the company is generally determined primarily by promoting the continued success of this business (*bestendig succes van de onderneming*). The Dutch Supreme Court added that, in discharging their duties, directors should also – partly based on the principle of reasonableness and fairness – exercise due care with regard to the interests of all those involved in the company and its business.

The management board of a BV/NV is accountable both internally and externally for the fulfilment of its duties and the exercise of the powers arising from the management task. Within the company, the management board has an accountability obligation towards the following.

- The general meeting:
 - (a) by preparing the annual accounts for shareholders;
 - (b) by publishing a management report; and
 - (c) by providing the general meeting with all requested information, unless this would be contrary to an overriding interest of the company.
- The supervisory board that supervises the management board.
- The works council.

Milieudefensie/Shell Case

The ruling of the District Court of The Hague of 26 May 2021 is relevant in this respect. An alliance of associations and foundations, together with over 17,000 individual claimants, brought a case against Royal Dutch Shell (RDS) as the top holding company of the Shell group, alleging that RDS had an obligation to contribute to the prevention of dangerous climate change through its corporate policies for the Shell companies.

The District Court found that, under Dutch law, RDS owed an unwritten standard of care to Dutch residents to reduce CO₂ emissions of the Shell group’s activities by net 45% by the end of 2030, relative to 2019. In doing so, the court took into account that there is a widely supported international consensus that human rights should be protected against the consequences of dangerous climate change, and that companies must respect human rights. The court also found that RDS’ policies, intentions and ambitions were incompatible with this reduction

obligation. Therefore, the court ordered RDS to comply. This is an obligation of result for the Shell group itself and a significant best-efforts obligation with regard to the Shell group's business relations and end-users.

On 12 November 2024, the Court of Appeal of The Hague overruled the judgment of the District Court. Though both courts agree that protecting against dangerous climate change is rooted in human rights, the Court of Appeal's decision sets out that a specific numerical reduction obligation – such as the 45% target – cannot be imposed on RDS based solely on an unwritten standard of care. Milieudefensie, has lodged an appeal against this ruling with the Supreme Court.

On 13 May 2025, Milieudefensie, announced that they intend to launch a second climate lawsuit against RDS. The organisation demands that RDS cease developing new oil and gas fields, arguing that these activities are incompatible with the urgent need to address the climate crisis. This new lawsuit would shift the focus from reducing emissions to halting the expansion of fossil fuel projects. Legal proceedings for this case are expected to begin soon, pending RDS's response.

Dutch Companies Within Scope of the CG Code

According to the CG Code, the management board must pay attention to the interests of stakeholders when developing a view on sustainable long-term value creation by the company and its affiliated business, and formulate a corresponding strategy.

The CG Code describes stakeholders as groups and individuals that, directly or indirectly, influence – or are or may be influenced by – the attainment of the company's objectives: employ-

ees, shareholders and other lenders, suppliers, customers and other stakeholders.

4.8 Consequences and Enforcement of Breach of Directors' Duties

General

In general, managing directors of a BV or NV are not liable for the obligations of the company they are managing. Directors have considerable liberty to act as they deem fit, but must properly perform their duties towards the company. They are jointly and severally liable for damage suffered if the management board performs its duties improperly (*onbehoorlijke taakvervulling*), based on the management board's collective responsibility. A distinction is made between the liability of directors towards the company (internal liability) and their liability towards third parties (external liability).

Internal Liability

The company may hold the managing directors liable for damage suffered by the company in the event of improper performance of duties (*onbehoorlijke taakvervulling*). To establish liability in such event, it must be proven that the managing director acted in a seriously culpable manner (*ernstig verwijtbaar*). This is generally the case if a managing director acts in breach of statutory provisions or in breach of the articles of association and gives rise to improper management, unless the managing director can prove otherwise.

In principle, if one managing director is in breach, all the managing directors are jointly and severally liable due to their collective liability. An individual managing director can be exonerated in the event that, also in view of the duties assigned to others, he does not bear any serious blame and he has not been negligent in taking measures to avert the consequences of improper

management. Supervisory directors may also be held liable for improper supervision.

In addition to liability for mismanagement, liability for damages may also be based on tort law (*onrechtmatige daad*). This concerns the liability of each director individually and not the collective liability of the board.

In an insolvency situation, the trustee may sue the directors on behalf of the company.

External Liability

Personal liability of a managing director towards third parties may arise if the managing director commits a wrongful act in their capacity as a director, or in the event of the bankruptcy of the company.

In a situation in which the company is liable for damages based on non-fulfilment of contractual or statutory obligations or a wrongful act, a managing director may in some cases also be held personally liable for the damages. A managing director is personally liable only if they bear serious personal blame (*ernstig persoonlijk verwijt*).

Serious personal blame on the part of a managing director generally exists if:

- the managing director knows or should have known that the company cannot fulfil the obligations under the agreement and nevertheless enters into an agreement on behalf of the company and knows and should have known that the company offers no recourse; or
- the managing director causes or allows the legal entity to fail to fulfil an existing obligation and offers no recourse.

External liability in bankruptcy

A managing director may be personally liable in the event of a company's bankruptcy. In a bankruptcy in which any claim remains unpaid, a bankruptcy trustee may hold directors liable for manifestly improper management (*kennelijk onbehoorlijk bestuur*) that was an important cause of the bankruptcy.

Manifestly improper management can be established if, among other things:

- the books and records (*administratie*) were improperly kept and the corresponding books, documents and other data carriers were not kept in such a way that the rights and obligations of the legal entity can be known at all times; or
- the company has failed to fulfil its duty to publish its annual accounts.

In these situations, it is assumed that manifestly improper management was an important cause of the bankruptcy. This assumption can be refuted by directors.

If a bankruptcy trustee's claim is successful, each managing director is jointly and severally liable in relation to the bankrupt estate for the deficit in the bankruptcy, being the amount of the liabilities to the extent that these cannot be satisfied by the liquidation of the other assets. Individual directors can be exonerated if they can demonstrate that they cannot be held liable for the manifestly improper management and that they did not fail to take measures to mitigate the consequences of the manifestly improper management.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other Bases of Liability of Directors

Managing directors of a BV/NV may also be jointly and severally liable in the following cases:

- for the debts of the company under social security and tax laws;
- for providing misleading (interim) accounts or annual accounts or annual reports; or
- for the company acquiring shares in its own capital in certain situations.

BV

In the case of a BV, the managing directors must give approval for each distribution before it can be made. If the company is unable to continue paying its debts after a distribution has been made, managing directors could be liable for any immediately payable company debts. Liability exists only if the directors knew or should reasonably have foreseen that the distribution would lead to the company being unable to continue paying its debts.

Limitation of Liability

In general, a managing director's liability may be limited in two ways.

- The general meeting discharges managing directors, waiving possible claims for damages. This concerns internal liability and is a common agenda item at the annual general meeting.
- Exoneration from joint and several liability of an individual managing director in the event of (manifestly) improper management in the case of joint and several liability of managing directors, if a director can demonstrate that they cannot be held liable for the (manifestly) improper management and did not fail to take

measures to mitigate the consequences of the (manifestly) improper management.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

BVs

The general meeting determines the individual remuneration of managing directors, unless the articles of association provide otherwise.

NVs

The general meeting determines the individual remuneration of managing directors, unless the articles of association provide otherwise. The articles of association of an NV may provide that another corporate body will determine the individual remuneration of managing directors, often the supervisory board. The remuneration of supervisory directors is always determined by the general meeting.

In addition, NVs must have a remuneration policy in place, which must be adopted by the general meeting. The works council must be given the opportunity to take a position thereon (or give its advice in the case of a Dutch listed company); this position (or advice) shall be offered to the general meeting at the same time as the proposal to adopt the remuneration policy.

Companies Within the Scope of the CG Code

For companies within scope of the CG Code, the following applies on “*comply-or-explain*” basis:

- the remuneration policy for the management board, prepared by the supervisory board's remuneration committee, should also focus on sustainable long-term value creation for the company and its affiliated business;
- severance pay is limited to one year's salary and will not be awarded if the managing

director resigns, or in the event of seriously culpable or negligent behaviour by the director; and

- supervisory directors must not be awarded remuneration in the form of shares and/or rights to shares.

4.11 Disclosure of Payments to Directors/Officers

Disclosure in Relation to Remuneration

Non-listed Dutch companies

These companies must publish the following in the notes to the annual accounts.

- The amount of the remuneration, including pension charges and other benefits, for:
 - (a) the managing directors and former managing directors; and
 - (b) separately, the joint supervisory and former supervisory directors (this provision does not apply to micro and small companies).
- The amount of loans, advances and guarantees granted for the benefit of individual directors and supervisory directors.

Dutch listed companies

Dutch listed companies must publish a remuneration report, which must:

- be clear and understandable;
- summarise all the remuneration awarded or due to individual directors in the previous financial year;
- be submitted to the annual general meeting for an advisory vote;
- be made public on the company's website after the general meeting and be accessible for ten years; and
- be checked by the external auditor as to whether all the required information is included in the report.

The company must explain in the remuneration report how the previous vote of the general meeting has been considered.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The management board manages the company; see **3.2 Decisions Made by Particular Bodies** and **4.6 Legal Duties of Directors/Officers**.

Shareholders provide the equity and, in principle, are liable only up to the amount of their investment in the company. They do not participate in most corporate decisions and may establish contractual arrangements with the company, such as relationships agreements.

See **3.2 Decisions Made by Particular Bodies** regarding the adoption of resolutions by the general meeting.

5.2 Role of Shareholders in Company Management

General

In general, shareholders are not involved in the management of the company.

The articles of association may stipulate that the management board must act in accordance with the instructions of a corporate body of the company (eg, the general meeting). The management board should assess whether the instruction is in the interest of the company and its affiliated business.

Role of the General Meeting

It follows from case law that the following applies to Dutch companies with respect to the role of

the general meeting and the policy and strategy of the company.

- The rule of law is that the management board, under the supervision of the supervisory board, is responsible for determining the policy and strategy of the company and its business.
- The management board is accountable to the general meeting in respect of its policy and strategy.
- The management board is not obliged to involve the general meeting in its decision-making in advance, nor to consult the general meeting; this is different if statutory provisions or provisions in the articles of association provide otherwise.
- The general meeting may express its opinions in this regard by exercising its powers prescribed by law or in the articles of association. Shareholders cannot force the company to include voting items, regardless of whether this is a binding or advisory vote, on the agenda of the general meeting in respect of matters that fall within the powers of the management board, such as determining the policy and strategy.

5.3 Shareholder Meetings

General

Both BVs and NVs must have one general meeting a year. The annual general meeting of an NV must be held within six months after the end of the company's financial year. The articles of association may provide for a shorter period. The annual general meeting of a BV must be held once a year, unless all shareholders are also directors of the BV. The signing of the annual accounts by all directors is also considered adoption of the annual accounts (the articles of association may provide otherwise).

Extraordinary Meeting

In addition to the annual general meeting, extraordinary meetings may also be convened for matters that come up between the annual meetings and need to be addressed in a general meeting.

Convening of a General Meeting

Both the management board and the supervisory board may convene a general meeting of an NV/BV (*bijeenroeping*). The articles of association may also grant this power to other parties.

Shareholders whose shareholding exceeds a certain threshold may request the board and supervisory board to convene a general meeting. If this request is denied, they can enforce in court that the general meeting be convened.

The general meeting is held at a place stated in the articles (for a BV, this can also be outside of the Netherlands) or in the municipality where the company has its place of business. A general meeting of an NV can also be held elsewhere if the entire share capital is represented or if, in the case of a BV, all persons with meeting rights agree to it. A Dutch bill is pending to allow general meetings to be held entirely virtually.

Digital Meeting

On 15 January 2024, the digital general meeting bill was submitted to the Dutch parliament. This bill provides the legal basis for a fully digital general meeting. The current regime only allows for a hybrid meeting, where the shareholder has the choice of either attending the physical meeting or exercising his/her meeting and voting rights remotely. Although the aim was for the new legislation to come into effect on 1 January 2025, this legislation is still pending. The date of entry into force has not yet been determined, but the bill is currently expected to be adopted on 1

July 2025 or 1 January 2026. It is therefore not yet possible to hold a fully digital shareholders' meeting.

Procedure at a General Meeting

Resolutions of the general meeting are adopted by absolute majority (*volstrekte meerderheid*) – ie, more than 50% of the votes validly cast. Certain resolutions are adopted by a qualified majority, as required by Dutch law or the articles of association.

In the case of an NV, each shareholder has at least one vote. In the case of a BV, deviations are allowed, and shares without voting rights may also be created.

In addition to shareholders with or without voting rights, other parties may also have meeting rights, which means they may attend and speak at the meeting.

Managing directors and supervisory directors have an advisory vote.

5.4 Shareholder Claims

The main proceedings through which shareholders can initiate legal proceedings against the company or directors are the inquiry proceedings (as described in the following). Shareholders can also have a board resolution nullified by the court or have it determined as void.

Inquiry Proceedings (*Enquêteprocedure*)

The Enterprise Chamber of the Amsterdam Court of Appeal (Enterprise Chamber) (*Ondernemingskamer*) has exclusive jurisdiction for these proceedings, which may be initiated, among others, by shareholders owning a certain percentage of the shares.

At the written request of the shareholder, the Enterprise Chamber may appoint one or more persons to conduct an investigation into the policy and affairs of the company. The Enterprise Chamber will only grant the request if there appear to be valid reasons to doubt a correct policy or course of action.

At any stage of the proceedings, at the request of the original applicants (the shareholder), the Enterprise Chamber may also order interim measures (*onmiddellijke voorziening*) for the duration of the proceedings. For example, it may temporarily appoint a managing director.

The report of the outcome of the investigation shall be filed at the registry of the Amsterdam Court of Appeal. Based on the report, the Enterprise Chamber may conclude that there has been mismanagement and order one or more of the following limitative provisions, which it considers appropriate based on the outcome of the investigation:

- suspension or annulment of a resolution of the directors, supervisory directors, general meeting or any other body of the legal entity;
- suspension or dismissal of one or more managing or supervisory directors;
- temporary appointment of one or more managing or supervisory directors;
- temporary departure from the provisions of the articles of association specified by the Enterprise Chamber;
- temporary transfer of shares for management purposes; and
- dissolution of the legal entity.

Dutch law does not recognise a derivative action.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Disclosure Obligations for Shareholders in Listed Companies

Anyone who acquires or disposes of a capital interest or the voting rights of a Dutch NV whose shares are listed on a regulated market within the European Economic Area (EEA), or a non-Dutch listed company whose shares are listed on a Dutch regulated market, must notify the AFM without delay if the percentage of capital interest or voting rights reaches, exceeds or goes under any of the following thresholds: 3%, 5%, 10%, 15%, 20%, 25%, 30%, 40%, 50%, 60%, 75% or 95%.

These thresholds may apply if shareholders obtain or lose ownership of shares (or related financial instruments) and/or votes, or due to an increase or decrease in the issued share capital of the listed company.

The same applies to anyone holding a gross short position in the company that reaches, exceeds or falls below any of the aforementioned thresholds.

The AFM publishes the notifications in its online registers.

In addition, the EU Short Selling Regulation contains disclosure obligations in respect of net short positions in EEA issuers.

Disclosure Obligations Applicable to Directors of Listed Companies

Managing directors and supervisory directors of Dutch NVs whose shares are listed on a regulated market in the Netherlands also need to notify the AFM of their shares and voting rights, and of any changes in these shares and voting rights concerning (rights to acquire) shares in the

issuing institution of which they are director and in affiliated issuing institutions.

Additional reporting obligations may apply under the EU Market Abuse Regulation.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Annual Reporting Obligations for BVs and NVs

The financial report consists of three parts:

- the management board report;
- the annual accounts; and
- other information – eg, the report of the external auditor.

The management boards of both BVs and NVs must publish their annual accounts and file them with the Dutch Trade Register no later than eight days after adoption by the general meeting. If the annual accounts have not been adopted within two months after the end of the period set for their preparation, the management must publish the annual accounts with a statement that they were not adopted.

In any event, annual accounts shall be filed within ultimately 12 months after the end of the financial year, regardless of whether or not they are adopted by the general meeting, together with other parts of the financial report. See **6.3 Companies Registry Filings** regarding filing requirements.

Dutch Listed Companies

Issuing institutions are subject to stricter financial reporting obligations under the Financial

Supervision Act and applicable EU regulations. These companies must, among other things:

- prepare and publish their annual financial report (including audited financial statements and management commentary) within four months after the end of the financial year; and
- publish half-yearly financial reports (including condensed financial statements and an interim management report) within three months after the end of the first six months of the financial year.

Both reports must be filed electronically with the AFM and made available to the public.

6.2 Disclosure of Corporate Governance Arrangements

General

Corporate governance arrangements that the managers of a Dutch listed company must implement to ensure compliance with the CG Code need to be disclosed in the management report. The management board describes the main risks and uncertainties to which the BV or the NV is exposed. The management report of large companies must also contain an analysis of both financial and non-financial performance indicators, including environmental and employment-related issues.

Dutch Listed Companies

Dutch listed companies must include additional information in the management report, including the following:

- the key features of the internal risk management and control systems in relation to the financial reporting process of the company and its consolidation group;

- the composition and performance of the management board, the supervisory board and their committees; and
- the diversity policy regarding the composition of the management board and the supervisory board.

Additional Information in Line With the CG Code

The CG Code provides that the company must explicitly state in a separate chapter of the management report (or a publication on the company's website) the extent to which it complies with the principles and best practice provisions of the CG Code and, where it does not comply, why and to what extent it deviates from these principles or best practice provisions.

According to the CG Code, the management board report must include a report on sustainable long-term value creation by providing information on the effects of the actions of the company and its affiliated business on people and the environment, a report on risk management, and explanatory notes on the culture within the company, the contribution of the culture and the values to the sustainable long-term value creation and the effectiveness and compliance with the code of conduct (see also **1.2 Sources of Corporate Governance Requirements** for more information on the CG Code).

Supervisory Board Report

The supervisory board report is mandatory only for Dutch listed companies and, pursuant to the CG Code, it must include:

- the role of the supervisory board, such as its involvement in the establishment of the strategy and the way in which it monitors its implementation;

- the independence of the supervisory board and of its directors and chair; and
- the way the evaluation of the supervisory board, its committees and the individual directors has been carried out.

6.3 Companies Registry Filings

Annual Accounts

Non-listed companies

The management boards of both non-listed BVs and NVs must publish their annual accounts and file them with the Dutch Trade Register, after which they will become publicly available.

The management board must prepare the annual accounts and make them available for inspection by shareholders at the company's offices within five months after the end of the financial year. The general meeting can extend this deadline by five months in exceptional circumstances.

The general meeting has two months to adopt the annual accounts after the period for preparing the annual accounts has expired. Within two months after that period has expired, the general meeting must adopt the annual accounts during a general meeting.

See **6.1 Financial Reporting** regarding the relevant filing deadlines and **5.3 Shareholder Meetings** regarding the timing of holding general meetings.

Dutch listed companies and large companies have to disclose complete financial statements. There are exemptions for medium, small and micro legal entities.

Dutch listed companies

Dutch listed companies whose securities are admitted to trading on a regulated market in the EU must make the annual accounts pub-

licly available and simultaneously file them with the AFM within four months after the end of the financial year.

The general meeting has two months to adopt the annual accounts, which also need to be filed with the Dutch Trade Register within eight days after they are adopted.

Please note that if the annual accounts have not been adopted within two months from the end of the period prescribed for preparation in accordance with the statutory requirements, the management board must immediately make the prepared annual accounts public.

Semi-annual accounts are only mandatory for Dutch listed companies

Issuing institutions whose securities are admitted to trading on a regulated market in the EU must publish and file semi-annual financial reports with the AFM, simultaneously, within three months after the end of the first six months of the financial year. This is in accordance with the Financial Supervision Act.

The AFM can impose an order subject to penalty for non-compliance and an administrative fine when these accounts are not filed in time.

Sanctions

Not filing the annual accounts on time is an economic crime, as stated in the Dutch Economic Offences Act. The penalty for this can range between paying a fine and prosecution. Not filing the annual accounts on time can also be proof of mismanagement, which could lead to the management board being personally liable for debt when a company is declared bankrupt on the basis of manifestly improper management (*kennelijk onbehoorlijk bestuur*). See also **4.8 Consequences and Enforcement of Breach of**

Directors' Duties for more information on external liability in bankruptcy.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Dutch corporate law requires an audit of the financial statements for all large and medium-sized companies.

The external auditor must examine whether the annual accounts provide the requisite legal disclosures and provide a true and fair view, whether other parts of the financial report comply with the statutory requirements and whether the management report conflicts with the annual accounts or contains any other material misstatements.

The external auditor reports on their audit to the management board and the supervisory board, and records the result of the audit in an independent auditor's report.

Appointment of the External Auditor

Book 2 of the Dutch Civil Code provides the following regarding the appointment of an external auditor:

- the general meeting appoints an external auditor;
- if the general meeting fails to do so, the supervisory board is authorised to make the appointment; and
- in the absence of a supervisory board, the management board is authorised to appoint the external auditor.

If an NV/BV is a public interest entity, the appointment must be notified to the AFM.

Further rules on the selection and appointment of auditors of public interest entities are included in Regulation (EU) 537/2014 on specific requirements regarding statutory audit of public interest entities (the "*Audit Regulation*") and in the CG Code. The audit committee plays an important role in preparing the appointment.

Public interest entities must regularly change audit firms.

An audit firm may not perform that function for more than ten consecutive years. The same firm may not carry out the statutory audit again until four years have passed. Within the relevant audit firm, the auditor responsible for the audit may not be responsible for the audit report for more than five years.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The management board is responsible for identifying and managing the risks associated with the company's strategy and activities.

The management board informs the supervisory board about the company's strategic policy, its general and financial risks and its internal control system at least once a year, to enable the supervisory board to perform its supervisory duties.

Additional Requirements for Dutch Listed Companies Based on the CG Code

The CG Code contains several best practices to further strengthen risk management and disclosure on "*comply-and-explain*" basis:

- a Dutch listed company must have adequate internal risk management and control systems;

- at least once a year, the management board must audit the operation of the internal risk management and control systems, and carry out a systematic review of their design and effectiveness;
- this monitoring covers all material control measures related to strategic, operational, compliance and reporting risks; and
- in performing their duties, the auditors must take into account the effectiveness of internal risk and control systems and the integrity and quality of financial reports.

Internal Audit Function

The internal audit function is responsible for assessing the design and operation of the internal risk management and control systems. The management board is responsible for the internal audit function. The supervisory board supervises the internal audit function and maintains regular contact with the person performing this function. The internal audit function reports hierarchically to a managing director, preferably the CEO.

In the management report, the management outlines the main risks and certainties to which the NV or BV is exposed. For a proper understanding of the results or position of the company and its group companies, the management report also includes, if necessary, an analysis of both financial and non-financial performance indicators, including environmental and employment-related issues.

NEW ZEALAND



Law and Practice

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Webb Henderson

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Webb Henderson specialises in corporate and M&A matters (including corporate governance, takeovers, joint ventures, partnerships and investment projects), as well as competition law and regulatory advice. Across its Auckland and Sydney offices, the firm comprises 17 partners and a total of 49 lawyers. The Auckland office is headed by partners Graeme Quigley and Garth

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1. Introductory

1.1 Forms of Corporate/Business Organisations

In New Zealand, the principal forms of business organisations are:

- bodies corporate – ie, legal persons separate from their owners, including:
 - (a) companies (formed under the Companies Act 1993);
 - (b) limited partnerships (formed under the Limited Partnerships Act 2008); and
 - (c) incorporated societies (formed under the Incorporated Societies Act 2022), which may not be formed for the purpose of pecuniary gain; and
- unincorporated forms – ie:
 - (a) partnerships (formed under the Partnership Law Act 2019); and
 - (b) trusts (formed under equitable principles, common law and the Trusts Act 2019).

Individuals may also carry on business in their own name - in which case, they are commonly referred to as “sole traders”.

1.2 Sources of Corporate Governance Requirements

The primary legislation that governs companies in New Zealand is the Companies Act 1993 (the “Companies Act”). On top of the requirements of the Companies Act, additional corporate governance requirements are imposed by:

- NZX’s Listing Rules (the “Listing Rules”) for issuers of listed securities; and
- industry-specific legislation (eg, for banks and insurers).

In the absence of any such additional requirements, the corporate governance arrangements applicable to a company are reasonably flexible. A company may add to, negate or modify many (but not all) of the governance provisions of the Companies Act by adopting a constitution that sets out the rules by which the company will be governed. Nevertheless, this chapter will describe the default position under the Companies Act - unless otherwise indicated.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies that have financial products quoted on the NZX Main Board or Debt Market must comply with the Listing Rules, which impose

requirements in relation to corporate governance – for example, requirements concerning the composition of the board, director remuneration, continuous disclosure, financial reporting, share issues, voting rights, and approval of major transactions.

The NZX also issues a Corporate Governance Code that takes effect on “*comply-or-explain*” basis, meaning that the issuer must either comply with the recommendations made in the Corporate Governance Code or explain:

- which recommendations were not followed;
- why, and in what period, those recommendations were not followed; and
- any alternative practice adopted in lieu of those recommendations (in which case, the issuer must confirm that this practice has been approved by its board).

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Recent areas of focus for corporate governance in New Zealand include director independence requirements, company law reform, shareholder activism, ESG reporting, climate-related financial disclosures and climate litigation (see **2.2 ESG Considerations**), and changes to the NZX capital-raising settings and guidance relating to major and related-party transactions (see **3.2 Decisions Made by Particular Bodies**).

As a result of a second round of consultation on its director independence settings, the NZX has amended the Listing Rules and Corporate Governance Code effective from 31 January 2025. The Listing Rules now require that where the board determines a director to be an “*independent director*” notwithstanding the presence of a

factor specified in the Corporate Governance Code which may give rise to “*disqualifying relationship*” (ie, non-independent status), an issuer of Quoted Equity Securities must publicly disclose the basis on which the relevant factor from the Corporate Governance Code was triggered, and why the board has determined that the relevant director is nevertheless independent.

The relevant changes to the Corporate Governance Code include:

- clarifying that in assessing whether there is “*disqualifying relationship*” as a result of the director receiving a substantial proportion of annual revenue from the issuer, the board must consider not only the director’s fees but also any distributions paid by the issuer to the director; and
- amending the audit committee composition recommendations such that one member must (i) have an adequate accounting or financial background, and (ii) be an “*independent director*”. The Corporate Governance Code contains guidance on determining whether the relevant person’s background is deemed to be adequate.

On 15 August 2024, the government announced a two-phase process of reforms to modernise and simplify company law in New Zealand. The first phase focuses on legislative reforms aiming to streamline the operation of the Companies Act, including expanding the ability to use modern technology to comply with Companies Act requirements. The bill containing these amendments is expected to be introduced to Parliament this year. For the second phase, the Law Commission has been tasked with conducting a review of directors’ duties and related issues of director liability, including issues raised by the Mainzeal litigation (see **4.6 Legal Duties of**

Directors/Officers). This review is expected to commence in 2025.

Over the last year, there has also been an observable increase in shareholder activism relating to the governance and performance of New Zealand publicly listed companies, including NZME, Vista Group and Fletcher Building, in addition to wider activism related to ESG factors (see 2.2 ESG Considerations).

2.2 ESG Considerations

In February 2024, the Supreme Court released its decision in *Smith v Fonterra & Ors* [2024] NZSC 5, declining to strike out a claim against a group of substantial New Zealand businesses. The claim was framed in terms of the existing recognised torts of public nuisance and negligence, and a proposed novel tort of “*climate system damage*”. The Supreme Court held that the claim under public nuisance was not “*bound to fail*” and should not be struck out, meaning that the matter may now proceed to a substantive hearing. The causes of action in negligence and “*climate system damage*” were consequently also not struck out, on the basis that to do so would not achieve “*material saving in hearing time or other court resources*”. In April 2025, the High Court declined an application by the defendants to join other greenhouse gas emitters to the proceedings, which the defendants had sought on the basis that their emissions had only an infinitesimal impact on global climate change.

The Smith proceedings are in keeping with the international trend of climate litigation against corporates. Three high-profile international examples of this are *Milieudefensie, v Shell*, *City of Chicago v BP* and *Notre Affaire à Tous* and others v BNP Paribas.

The Corporate Governance Code and the NZX’s ESG Guidance Note place greater emphasis on ESG factors and clarity of reporting by listed issuers on such matters. The Corporate Governance Code features a recommendation that issuers provide non-financial disclosures (including in relation to “*environmental, social sustainability and governance factors and practices*”) at least annually, and supports the use of recognised international reporting initiatives for this purpose where appropriate to the company’s scale. The Listing Rules also specify that annual reports of NZX-listed entities must contain either:

- a copy of climate statements prepared by the entity in accordance with the requirements of the Financial Markets Conduct Act 2013; or
- the address of, or a link to, the website where a copy of those statements can be accessed.

In addition, a range of regulatory inquiries in New Zealand and Australia over recent years have emphasised the importance of institutional culture in mitigating the risk of misconduct or undesirable outcomes for consumers, namely:

- the Australian Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry;
- the Australian Prudential Regulation Authority (APRA)’s Prudential Inquiry into the Commonwealth Bank of Australia; and
- the Financial Markets Authority and the Reserve Bank of New Zealand’s joint review of the conduct and culture in New Zealand banks and the insurance industry, which has resulted in the introduction of a new licensing regime relating to “*conduct of financial institutions*”.

The reports from these inquiries emphasised that boards of directors are expected to take owner-

ship of organisational culture and set the “*tone from the top*”, as part of their wider responsibility for risk management.

The Financial Sector (Climate-Related Disclosures and Other Matters) Amendment Act 2021 makes specified disclosures concerning climate change and emissions governance, strategy, risk management and metrics/targets mandatory for a range of financial institutions (including large, listed entities) for financial years commencing from 1 January 2023 onwards.

The Listing Rules require listed issuers to report the gender balance of their directors and officers, along with a performance review of the issuer’s diversity policy.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies or functions involved in the governance and management of a company are its shareholders, its board of directors, and the company’s management team, if it has one. (It is common for boards of directors to appoint senior employees to management positions and delegate the necessary authority for managing the day-to-day affairs of the business to those senior employees – see **3.2 Decisions Made by Particular Bodies**.)

3.2 Decisions Made by Particular Bodies

Under the Companies Act, shareholder approval is required for certain significant matters such as adopting or altering the constitution, approving an amalgamation of the company with one or more other companies, commencing a voluntary liquidation, and “*major transactions*”. Major transactions under the Companies Act are, in

broad terms, those in which the company proposes to acquire or dispose of assets, rights or interests (or incur obligations or liabilities) – the value of which is more than half the value of the company’s assets immediately prior to the transaction. The company law reforms referred to in **2.1 Hot Topics in Corporate Governance** are expected to include clarification that straightforward transactions affecting share capital (such as the issue of new shares for cash), for which the Companies Act contains separate approval regimes, are not “*major transactions*”.

In addition, for NZX-listed entities, the Listing Rules require shareholder approval for material transactions with related parties and some categories of major transactions. NZX’s Major and Related Party Transactions Guidance Note was recently updated, including to reflect a policy shift on the part of NZX such that waivers from the relevant Listing Rules are now likely to be more difficult to obtain (the focus is on preserving shareholders’ rights to vote on such transactions).

Other decisions are left to the board. The board may delegate its powers to a director, a committee of directors, an employee or any other person – although the board remains responsible for monitoring the decisions made by its delegate. There are, however, some powers that may not be delegated by the board. These are set out in Schedule 2 to the Companies Act and include issuing new shares, authorising dividends or other distributions, and acquiring the company’s own shares.

3.3 Decision-Making Processes

A shareholder resolution may be passed at a shareholders’ meeting (see **5.3 Shareholder Meetings**) or by written resolution.

When shareholders exercise a power reserved to them by the Companies Act or the company's constitution, the power is exercised by ordinary resolution (ie, a simple majority of votes cast on the resolution) unless otherwise specified in the relevant provision of the Companies Act or constitution. Some matters require approval by way of “*special resolution*”, meaning that – if the resolution is to be passed at a meeting – a majority of at least 75% of votes cast must be obtained to pass the resolution. That threshold may be increased (but not lowered) by the company's constitution.

For a written (circular) resolution of shareholders, the resolution must be signed by not less than 75% of the shareholders entitled to vote, who must together hold not less than 75% of the votes entitled to be cast on the resolution. A copy of such a written resolution must be sent within five working days to all shareholders who did not sign it.

Decision-Making by Directors

Directors may also make decisions by way of resolutions passed at meetings or by written resolution. Schedule 3 to the Companies Act sets out the default rules for directors' meetings, including:

- requirements for notice (two business days);
- the required quorum (a majority of directors);
- means of attendance (in person or by audio or audiovisual communication); and
- voting (only a majority decision by directors present at the meeting is required, with each director having one vote – the chair does not have a casting vote).

The board must ensure that minutes of all directors' meetings are kept.

Directors may also pass a written (circular) resolution. Unless the company's constitution specifies otherwise, this must be signed or assented to by all the directors entitled to receive notice of a directors' meeting.

4. Directors and Officers

4.1 Board Structure

Under the Companies Act, companies have a single board. Boards may appoint committees to take responsibility for particular aspects of the business or the governance of the company, and the Listing Rules require listed companies to have an audit committee. The Corporate Governance Code also recommends that listed companies have a remuneration committee and a nomination committee.

4.2 Roles of Board Members

The Companies Act only provides for one class of director, meaning that all directors have the same fundamental role. However, in practice, committee memberships can mean that directors are more involved in certain aspects of the business or its governance than other areas. In addition, the company's constitution may (if desired) specify different categories of directors. Usually, the board will elect a chair. The default position under the Companies Act is that the chair does not have a casting vote.

4.3 Board Composition Requirements/Recommendations

The Companies Act requires every company incorporated in New Zealand to have at least one director that lives in either New Zealand or an “*enforcement country*”. If living in an enforcement country, the director must also be a director of a body corporate that is incorporated in that enforcement country under a law equivalent

to the Companies Act. At present, Australia is the only approved “*enforcement country*”.

The constitution of a company may increase the minimum number of directors.

The Listing Rules require listed companies to have at least three directors – two of whom must ordinarily reside in New Zealand and two of whom must be independent directors. The Corporate Governance Code further recommends that the majority of the board be independent directors.

“*Independence*” in this context is assessed having regard to the factors outlined in the Corporate Governance Code. Broadly, “*independent*” for this purpose means directors who are free of any interest, position, association or relationship that could reasonably be perceived to materially influence their capacity to:

- bring an independent view;
- act in the company’s best interests; and
- represent the interests of the company’s financial product holders generally.

Industry-specific legislation may impose stricter obligations on the board composition of a company in that industry. For example, the Reserve Bank of New Zealand’s Banking Supervision Handbook for the banking sector and its governance guidelines for the insurance sector both require at least half of the company’s directors to be independent.

4.4 Appointment and Removal of Directors/Officers

Section 153 of the Companies Act provides that, unless varied by the company’s constitution, directors are appointed by ordinary resolution (a simple majority of votes) of the shareholders.

In addition, the court has the power to appoint directors upon the application of a shareholder or creditor if there are no directors – or fewer directors than the quorum for a board meeting – and it is not possible or practicable to appoint directors in accordance with the company’s constitution. A director may be removed by an ordinary resolution of shareholders at a meeting called for purposes that include the removal of the director (in which case, the notice of meeting must state this).

These provisions may be modified by the constitution. In an incorporated joint venture, for example, it is common for each party to be able to appoint and remove a specified number of directors – regardless of whether that shareholder is entitled to exercise more than 50% of the votes at a shareholder meeting.

4.5 Rules/Requirements Concerning Independence of Directors

Directors are restrained from acting in situations where their personal interests may conflict with the interests of the company. Section 131 of the Companies Act requires a director to act in good faith and in what the director believes to be the best interests of the company when exercising powers or performing duties – see **4.6 Legal Duties of Directors/Officers**.

Section 139 of the Companies Act further defines a director as “*interested*” in a transaction of the company if, in broad terms, the director:

- is a party to – or will or may derive a material financial benefit from – the transaction (or is a director, officer, trustee, parent, child, spouse, civil union partner or de facto partner of such a person);
- has a material financial interest in another party to the transaction; or

- is otherwise directly or indirectly materially interested in the transaction.

A director who is interested in a transaction with the company must disclose that interest to the board immediately after becoming aware that they are interested in the transaction – except where the transaction is in the ordinary course of the company’s business and on its usual terms. Such disclosure must be entered in the interests register, including the nature and monetary value of the interest or the extent of the interest (if not quantifiable). A director may disclose an ongoing interest in a named person or company, with the effect that the director will be treated as having disclosed an interest in any future transaction with that person or company.

Failure to disclose an interest does not invalidate the transaction but does allow the company to avoid the transaction at any point during the first three months following the disclosure of the transaction to all shareholders if the company did not receive fair value (based on the knowledge of the company and the interested director at the time the transaction was entered into). Where the property has been transferred on to a third party, the company’s right to avoid the transaction does not affect the title or interest of that third party if they are a purchaser for valuable consideration without knowledge of the circumstances under which the first person acquired the property.

The default position under the Companies Act is that an interested director may vote on matters relating to the transaction, be counted in the quorum, and otherwise do anything as though the director were not interested in that transaction. However, boards often adopt charters or codes of conduct that record their collective expectations as to how conflicts of interest

(which may be more broadly described than the formal definition of “*interested*” contained in the Companies Act) will be managed. Those charters or codes of conduct commonly provide that directors with an actual or potential conflict of interest will abstain from participating in meetings and voting on matters in respect of which the conflict exists – an approach that directors of listed companies are also required to follow under the Listing Rules.

A director is also subject to restrictions on the disclosure and use of company information where that information is obtained in their capacity as a director or an employee of the company and would not otherwise be available to them. A director may, unless prohibited by the board, disclose such information to a person whose interests the director represents or a person in accordance with whose directions the director is required or is accustomed to act (see **5.2 Role of Shareholders in Company Management**). These exceptions contemplate the concept of a nominee director – ie, a director nominated by a shareholder to represent its interests on the board of the company. In the latter case, the name of the person to whom the information is disclosed must be entered in the interests register.

Alternatively, a director may disclose or make use of such information if:

- the board approves the disclosure or use;
- the disclosure or use will not, or will not be likely to, prejudice the company; and
- particulars of the disclosure or use are entered in the interests register.

When a director of a company acquires or disposes of “*relevant interest*” in shares issued by that company, the director must disclose to the

board the number and class of shares in which the relevant interest was acquired or disposed of, the nature of the director's relevant interest, the consideration, and the date of the transaction. That information must be entered in the interests register. A director has a relevant interest in a share if:

- the director is the beneficial owner of the share; or
- the director may exercise (or control the exercise of):
 - (a) the power to vote; or
 - (b) the power to acquire, or dispose of, the share.

In the case of a listed company, its directors and senior managers are required to also publicly disclose any acquisition or disposal of “*relevant interest*” in the company's (and its related bodies corporates') quoted financial products.

A director must not trade in an unlisted company's shares or other financial products if the director possesses information material to an assessment of the financial products' value that they would not be in possession of but for their position as director or employee – unless the director pays no less or receives no more than the fair value of the financial products. Otherwise, the director is liable to the counterparty for the difference between fair value and the consideration.

As regards the quoted financial products of a listed company, the insider trading provisions of the Financial Markets Conduct Act 2013 (FMCA) apply instead. In general terms, these provisions prohibit persons (including directors) who have “*inside information*” from:

- trading quoted financial products;

- encouraging or advising other persons to trade or hold those financial products (or to advise or encourage a third person to do so); or
- disclosing the inside information.

In this context, “*inside information*” refers broadly to information that:

- is not generally available to the market (but that a reasonable person would expect to have a material effect on the price of the relevant financial products were it generally available to the market); and
- relates to particular financial products or issuers (rather than to financial products or issuers generally).

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors under the Companies Act are described in the following sections. Directors also have a number of administrative obligations, including those relating to disclosure of their interests and share dealings (see 4.5 Rules/Requirements Concerning Independence of Directors), as well as an obligation to supervise the maintenance of the company's share register and obligations to ensure relevant filings are made with the Companies Office.

Section 131 – Good Faith and Best Interests of the Company

As mentioned in 4.5 Rules/Requirements Concerning Independence of Directors, a director is required to act in good faith and in what the director believes to be the best interests of the company when exercising their powers or duties. This test is subjective – ie, it relies on the director's belief, rather than what is objectively in the company's best interests (Madsen-Ries and Levin as Liquidators of Debut Homes Limited (in liquidation) v Cooper [2020] NZSC 100 at [112]) –

although “directors will probably have a hard task persuading the court that they honestly believed that an act or omission that resulted in substantial and foreseeable detriment to the company was in the company’s best interests” (at [109]). Under a subjective test, however, “the fact that an allegedly unreasonable belief was held may... provide evidence that the belief was not honestly held” (at [109]). Case law and commentary has also identified exceptions to the subjective nature of the test where there is no evidence of actual consideration of the best interests of the company, where there is a failure to consider the interests of creditors in an insolvency or near-insolvency situation, where there is a conflict of interest, or where a director’s decisions are irrational (at [113]).

If provided for in the company’s constitution and (in some cases) agreed to by the other shareholders, a director may act in the best interests of a parent company or – in the case of a joint venture – their appointing shareholder, even though such actions may not be in the best interests of the company. In the absence of such a provision in its constitution, the interests of a company must be considered separately from the interests of a group of related companies (*Kumar v Smartpay Ltd* [2023] NZCA 410).

Section 131 was amended in 2024 to expressly state that as part of directors’ duty to act in good faith and in what they believe to be the best interests of the company, directors may consider matters other than the maximisation of profit, and gives as examples “*environmental, social, and governance matters*”. As part of the reforms to New Zealand company law discussed at **2.1 Hot Topics in Corporate Governance**, it is proposed that this amendment be reversed, on the basis that it was already clear that directors are free to consider matters other than the

maximisation of profit, and that referring to specific matters in the Companies Act may raise questions about the weight that may be given to other matters. The earlier amendment had also attracted criticism noting that (as an unintended consequence) it appeared to presuppose that directors must consider the maximisation of profit, whether or not they also consider the other matters referred to.

Section 133 – Proper Purpose

Directors must exercise their powers for a proper purpose – that is, when exercising a power conferred upon them, the director must exercise that power in line with the purpose for which it was conferred. This duty is distinct from the duty in respect of best interests, as it is possible to exercise a power for an improper purpose even if the director genuinely believed the course of action was in the best interests of the company.

Section 134 – Compliance With Companies Act and Constitution

A director may not act, or agree to the company acting, in a way that contravenes the Companies Act or the company’s constitution. A contravention of another statute would not necessarily breach this duty, but may breach Section 131 (with regard to good faith and best interests of the company) and Section 133 (with regard to proper purpose).

Section 135 – Reckless Trading

A director must not agree to the business of the company being carried on – or cause or allow the business of the company to be carried on – in a manner likely to create a substantial risk of serious loss to the company’s creditors. Whether or not a director believes the conduct of the business is reasonable is irrelevant. Directors are required to make “*sober assessment*” of whether their future trading forecasts justify

continuing to trade and whether the assumptions that underpin those forecasts are reasonable (*Mason v Lewis* [2006] 3 NZLR 225 at [51]); however, the benefit of hindsight should not be applied to directors' decisions. If there is not a reasonable prospect of the company regaining solvency, formal insolvency mechanisms should be invoked (see *Debut Homes*) – it is not enough that the director's decisions would reduce the overall deficit. Directors may not continue to trade in a way that favours one class of creditors over another.

In the long-running Mainzeal litigation, the Supreme Court has upheld the finding of the Court of Appeal that four former directors of Mainzeal (a construction company) breached Section 135 (*Yan v Mainzeal Property and Construction Limited* (in liquidation)). In this case, money was extracted from Mainzeal to an overseas parent company through intermediary companies that were insolvent. A director of both Mainzeal and its parent company made representations to his fellow directors that the parent company would financially support Mainzeal when it first became insolvent in a balance sheet sense. The representation was not legally binding and the parent company did not provide the support when it was needed. The directors were found to have exposed creditors to substantial risk of serious loss by continuing to trade in reliance on the non-binding representations and without a substantial capital injection. However, the court did not award compensation in respect of the breach of Section 135, because the court held that the directors' conduct during the relevant period did not increase the aggregate loss suffered by Mainzeal's creditors – known as the “*net deterioration*” approach.

Section 136 – Obligations

A director must not agree to the company incurring an obligation unless the director believes at the time, on reasonable grounds, that the company will be able to perform the obligation when it is required to do so. Indications that this belief is reasonable may include:

- the fact that the company is able to continue trading for a reasonable time following the incurring of the obligation;
- the fact that bank finance is still available to the company; and
- the fact that any downturn in the company's performance was unexpected or sudden.

Factors that count against the belief being reasonable include incurring long-term liabilities before the business of the company has been successfully established or incurring obligations following the loss of an important revenue stream.

In the Mainzeal case, the Court of Appeal held that:

- Mainzeal had used funds owed to subcontractors as working capital in order to continue to trade;
- Mainzeal entered into large construction contracts without the company's directors having reasonable grounds to believe it would be able to perform the contracts through to completion; and
- the directors breached Section 136 in agreeing to the company doing so.

The Supreme Court agreed with the Court of Appeal's approach and found that compensation for breaches of Section 136 should be assessed on “*new debt*” basis (ie, debt incurred once the directors did not have reasonable grounds to

believe that the company would be able to perform the new obligations).

Section 137 – Duty of Care

A director of a company, when exercising powers or performing duties as a director, must exercise the care, diligence and skill that a reasonable director would exercise in the same circumstances – taking into account (without limitation) the nature of the company, the nature of the decision, and the position of the director and the nature of the responsibilities undertaken by them.

This section does not automatically impose a higher standard of skill on directors who hold professional qualifications in a particular area. The position may, however, be different if a director is brought onto the board to add a particular skill set.

Section 138 – Use of Information and Advice

The Companies Act expressly permits directors, when exercising powers or performing duties, to rely on reports, statements, financial data, professional and expert advice, and other information provided by:

- those (including employees, professional advisers and experts) whom the director reasonably believes to be competent in the relevant area; and
- fellow directors (or directors' committees on which the director did not serve) in relation to matters within those directors' or committees' designated authority.

In each case, the director must act in good faith, have no knowledge that such reliance is unwarranted, and make proper inquiry where the need for inquiry is indicated by the circumstances.

Mainzeal Implications

The Supreme Court also noted the following implications arising out of the Mainzeal case:

- directors have a continuing obligation to monitor the performance and prospects of the company;
- where monitoring reveals the potential for substantial risk of serious loss to creditors or doubt as to whether there exists a continuing reasonable basis for the belief that obligations incurred will be able to be honoured, directors should squarely address the future of the company;
- directors may need to obtain independent expert advice and the courts will allow a reasonable time for directors to “take stock” and decide on a course of action;
- directors must deal directly with the issues giving rise to the concern, recognising that a long-term strategy of trading while balance sheet insolvent is generally not acceptable; and
- courts will apply a standard of reasonableness when assessing directors' decisions, noting that:
 - (a) these decisions are likely to involve the exercise of business judgement; and
 - (b) directors are often required to make complex decisions under the pressure of time with incomplete knowledge despite their best efforts, and the courts will avoid “hindsight bias” (ie, will recognise that reasonable decisions may nonetheless turn out badly and there may be more than one reasonable course of action).

4.7 Responsibility/Accountability of Directors

All the directors' duties described in 4.6 **Legal Duties of Directors/Officers** are owed to the company, rather than to shareholders. A limited

set of duties is owed directly to the shareholders, including the duty to supervise the share register and the duty of directors to disclose their interests and dealings in the company's shares.

Although directors owe none of these duties directly to creditors, Section 135 and Section 136 respectively require directors to consider whether the company's business is being carried out in a way that is likely to create a substantial risk of serious loss to creditors and whether the company will be able to perform the obligations that it proposes to incur.

If the company became insolvent and was placed into liquidation, the liquidator could then bring an action (on behalf of the company) against a director that had breached their duties to the company. Amounts received from directors as a result would be applied for the benefit of the company's creditors in the liquidation.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Shareholder Enforcement

A present or former shareholder may bring an action against a director for a breach of duty owed to them as a shareholder (Section 169), but may not directly bring an action against a director for breaches of duties owed to the company.

However, Section 165 allows a shareholder or director to apply to the court for leave to bring proceedings in the name and on behalf of the company. This creates an avenue for shareholders to hold directors to account for breaches of their duties to the company (and may also be used for bringing proceedings against third parties). The Section may also be used to intervene in existing proceedings for the purpose of con-

tinuing, defending or discontinuing proceedings to which the company is a party.

When determining whether to grant leave to the shareholder (or director), the court must have regard to:

- the likelihood of success;
- cost;
- anticipated level of relief;
- any action already taken to obtain relief; and
- the interests of the company in the proposed proceedings.

The court should also consider whether the applicant seeking leave may have ulterior motives other than the best interests of the company (*Johnson v Johnson* [2020] NZHC 1563). In *Vijayakumar v Vasanthan* [2021] NZHC 1827, the court noted that it was helpful in this respect to consider whether an experienced liquidator would bring the claim, given that they regularly decide whether to issue proceedings against directors.

Additionally, the court may decline an application under Section 165 if a more effective alternative remedy exists under Section 174. Leave will only be granted if the court is satisfied that:

- the company does not intend to bring, diligently continue or defend, or discontinue the proceedings itself; or
- it is in the interests of the company that the proceedings should not be left to the directors or to the determination of the shareholders as a whole.

Sections 170 and 172 allow a shareholder to bring an action requiring a director or the company to take any action required to be taken by the directors or the company (respectively)

under the Companies Act or the company's constitution.

In any of the above-mentioned proceedings, the court may appoint a shareholder to represent all other shareholders where the shareholders have the same or substantially the same interest (Section 173). The purpose of this provision is to avoid numerous proceedings in which the dispute in each case is essentially the same.

A present or former shareholder (or any other person on whom the constitution confers the rights of a shareholder) is also entitled to take action against the company in situations where the shareholder or person considers that the “*affairs of the company*” have been or are being or are likely to be conducted in a manner that is oppressive, unfairly discriminatory or unfairly prejudicial to them in that capacity or in any other capacity (Section 174). The reference to conduct of the “*affairs*” of a company has been interpreted broadly, encompassing any conduct that generally concerns the company. However, this does not include actions of directors or shareholders in a purely personal capacity (*Van der Fluit v O'Neill* [2021] NZHC 1651). Non-compliance by the company or directors with specified provisions of the Companies Act is deemed to be conduct of that kind, as is the provision of a certificate by a director without reasonable grounds for an opinion set out in that certificate. (Directors are required to certify prescribed matters in respect of decisions to, for example, issue shares or pay dividends or other distributions or so that the company can acquire its own shares.) The court may grant a wide range of remedies in response to a successful application under this provision.

What constitutes oppressive, unfairly discriminatory and unfairly prejudicial conduct was con-

sidered by the Court of Appeal in *Thomas v HW Thomas Limited* [1984] 1 NZLR 686 at [694]. It was said in this case that the three terms were not to be read as distinct but, rather, as overlapping terms that help to explain one another. The Court of Appeal in *Latimer Holdings Limited v Sea Holdings NZ Limited* [2005] 2 NZLR 328 at [138] further elaborated that “*unfairness requires a visible departure from the standard of fair dealing, assessed in light of the history and structure of the company and the expectations of its members*”.

In *Wilding v Te Mania Livestock* [2017] NZHC 717, the High Court held that:

- conduct need not be unlawful to be oppressive;
- the inquiry concerns the effect of the conduct, not the intention of the parties;
- the “*just and equitable*” aspect means plaintiffs should not have acted wrongly; and
- remedies afforded under the section should be designed to best advantage shareholders as a whole.

A fairly calculated buyout offer made by the other parties involved may be viewed as curing unfair or prejudicial conduct (*Birchfield v Birchfield Holdings Ltd* [2021] NZCA 428).

Company Enforcement

The company may bring an action against one or more of its directors or former directors for breach of a duty owed by that director to the company. As the business and affairs of the company must be managed by – or under the direction or supervision of – its board, it falls to the board to decide whether such an action should be brought. If the directors do not resolve to do so (eg, if the majority of the board was complicit in the breach), a shareholder or direc-

tor can apply to the court for leave to bring an action on behalf of the company in the above-mentioned manner.

Consequences

Breaches of the above-mentioned directors' duties generally attract civil liability (although a number of the administrative provisions of the Companies Act attract criminal liability). The following are two key exceptions.

- Section 138A creates an offence for serious breaches of the duty of good faith. Such a breach will occur when a director, during the course of exercising their powers, acts in bad faith towards the company, believes that the conduct is not in the best interest of the company, and knows that the conduct will cause serious loss to the company. *"In short, the offending requires dishonesty"* (see *Spence v R* [2021] NZCA 499 at [36]).
- Section 380 creates an offence for dishonestly failing to prevent a company from incurring a debt where the director knows that the company is already insolvent or will become insolvent as a result of incurring the debt.

The court may also disqualify an individual from being a director in certain circumstances, including for persistent failure to comply with relevant laws or for acting in a reckless or incompetent manner in the performance of the director's duties, or upon conviction of certain offences or crimes involving dishonesty.

In the course of a liquidation of the company, liquidators, creditors and shareholders also have limited powers to apply to the court to order a director (or a promoter, manager, administrator, liquidator or receiver) to repay or restore money or property under Section 301 if that person has:

- misapplied, retained, or become accountable for that money or property; or
- been guilty of negligence, default or breach of duty or trust in relation to the company.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

The key enforcement avenues that are generally applied in respect of corporate governance requirements in New Zealand are described in **4.8 Consequences and Enforcement of Breach of Directors' Duties**. However, there are other potentially relevant enforcement avenues, including the following.

- The Financial Markets Authority (a regulator) may apply to the court for management banning orders that prohibit individuals from engaging in certain activities with regard to the governance and management of companies.
- The Reserve Bank of New Zealand may remove directors of licensed insurers from their positions if it is not satisfied that they are fit and proper persons to hold those positions. It may also remove directors of banks if specific criteria are met.

Limitations on Liability of Directors

Section 162 of the Companies Act allows a company to effect insurance on behalf of – and to indemnify – its directors, subject to specific limits and exclusions.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The board may authorise the payment of remuneration (or compensation for loss of office) and provision of other benefits (eg, loans and guarantees) to directors. However, before doing so, the board must be satisfied that any such action

is fair to the company. Any director who votes in favour must sign a certificate to this effect that also sets out the grounds for their opinion. Such grounds must be reasonable. If these requirements are not satisfied, the director receiving the payment or other benefit is liable to the company for the payment or benefit unless they prove that it was fair to the company.

For listed companies, the Listing Rules require directors' remuneration – and any increase in such remuneration – to be approved by ordinary resolution. Failure to do so is a breach of the Listing Rules and action may be taken in accordance with the enforcement policy of NZ RegCo (NZX's independently governed regulatory arm). The Corporate Governance Code also recommends that listed companies have a remuneration committee – the functions of which include recommending to shareholders (for their approval) the appropriate remuneration for directors.

4.11 Disclosure of Payments to Directors/Officers

Directors' remuneration (or any other benefit covered by Section 161) must be entered in the company's interests register, which must be made available for inspection by shareholders in the company.

For listed companies, the Corporate Governance Code also recommends that issuers have a publicly available remuneration policy in which the components of director remuneration are clearly separated. Director remuneration should be fully disclosed to shareholders in the issuer's annual report, including a breakdown of remuneration for committee roles and for fees and benefits received for any other services provided to the issuer.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

A company has separate legal personality from its shareholders. Unless the company's constitution provides otherwise, shareholders are not liable for the company's obligations merely because they are shareholders. As such, their liability to the company is limited to amounts unpaid on their shares, liability for breaches of duty if they act as "*deemed directors*" of the company, recovery of unauthorised distributions, and liability provided for in the constitution (eg, for capital calls on shares).

The constitution of the company is binding as between the company and the shareholders and as between the shareholders (Section 31). It is also common for shareholders in more closely held companies to enter into shareholders' agreements that govern the conduct of shareholders and are distinct from the constitution. The key advantage of such an agreement is that it does not have to be disclosed – whereas the constitution must be filed with the Companies Office in its electronic registry, which is freely searchable by the public. The shareholding details of a company's ten largest shareholders (or, if it is not a publicly listed company, all shareholders), as at the date of the company's last annual return, are also publicly available on the Companies Office website.

5.2 Role of Shareholders in Company Management

Although the business and affairs of the company must be managed by – or under the direction or supervision of – the board of the company, some particularly important decisions are reserved for the shareholders of the company. These include:

- a decision to approve “*major transaction*” (see **3.2 Decisions Made by Particular Bodies**) by special resolution;
- the appointment and removal of directors by ordinary resolution; and
- a decision to amalgamate the company with another company (apart from members of the same wholly owned group) or to commence a voluntary solvent liquidation, each by special resolution.

The chair at a shareholders’ meeting must allow a reasonable opportunity for shareholders to question, discuss or comment on the management of the company. The shareholders are entitled to pass a resolution relating to the management of the company but, unless the constitution provides otherwise, such a resolution is not binding on the board.

In addition, the company’s constitution may confer powers upon shareholders that would otherwise be exercised by the board (Section 126 (2)). A shareholder that exercises, or takes part in deciding whether to exercise, that power is deemed to be a director and subject to the directors’ duties contained in Sections 131 to 138 in relation to that action. Similar provisions apply where the constitution of a company requires a director or the board to exercise or refrain from exercising a power in accordance with a decision or direction by shareholders or, as mentioned in **4.5 Rules/Requirements Concerning Independence of Directors**, where a director or the board is accustomed to acting or required to act in accordance with another person’s directions or instructions.

5.3 Shareholder Meetings

The board of a company is required to call an annual meeting of shareholders unless:

- there is nothing required to be done at that meeting;
- the board has resolved not to call or hold the annual meeting; and
- the company’s constitution does not require such a meeting.

The board, or any other person authorised by the constitution, may call a shareholders’ meeting at any time. Such a meeting must be called on the written request of shareholders holding shares carrying together not less than 5% of the voting rights.

Schedule 1 to the Companies Act sets out the default rules for proceedings at shareholders’ meetings, as outlined below. Some of these may be modified by the company’s constitution.

Written notice of a meeting must be given to each shareholder, director and auditor at least ten working days prior to the meeting. The notice must specify the time, the place and the nature of the business to be transacted at the meeting, in sufficient detail to enable a shareholder to form a reasoned judgement in relation to it. Where any special resolution is to be submitted to the meeting, the text of that resolution must be included in the notice.

Shareholders may attend in person or via audio or audiovisual communication (ie, an electronic meeting). Electronic meetings have become increasingly common following the emergence of COVID-19 and are specifically provided for in the Companies Act (Schedule 1) and the Listing Rules (Rule 2.14.3). Shareholders may also appoint a proxy to attend the meeting on their behalf or – if permitted by the constitution – cast “*postal vote*”, including by electronic means. The quorum requirement will be met if those attending, together with those voting by proxy or by

postal vote, are entitled to exercise a majority of the votes entitled to be cast.

If the directors have elected a chair of the board, that person must chair the meeting if they are present. If the chair is not present within 15 minutes, the shareholders present may choose one of their number to chair the meeting.

For meetings held in person, the default method for voting is by a show of hands or by voice. For meetings via audio or audiovisual communication, the chair may decide how a vote is to be conducted. In each case, the number of shareholders who have voted for or against each resolution by postal vote is also counted. Any five shareholders, the chair, or shareholders who together hold 10% of the votes may require a poll to be conducted – in which case, votes must be counted according to the number of votes attached to the shares held by the relevant shareholders.

Postal votes must be received by the person authorised to receive and count them (or, if there is no such person, any director) at least 48 hours prior to the meeting.

The board must ensure that minutes are kept of all proceedings at shareholders' meetings. Minutes that are signed as correct by the chair are prima facie, evidence of the proceedings.

Shareholders may raise matters for discussion or resolution at the next meeting of shareholders. The Companies Act specifies the timeframes that must be met by a shareholder who proposes to do so and how the cost of giving notice of those matters to all shareholders will be met (ie, whether by the proposing shareholder or the company).

5.4 Shareholder Claims

See 4.8 Consequences and Enforcement of Breach of Directors' Duties.

Dissenting shareholders also have what is commonly known as "*minority buyout right*" if certain proposals are approved by shareholders and the dissenting shareholder votes against the proposal. The relevant categories of proposal are:

- an alteration of rights attached to shares in the company;
- adopting, revoking or changing the company's constitution in a way that imposes or removes a restriction on the activities of the company;
- amalgamating the company with another company; or
- entering into a major transaction.

In such a case, the dissenting shareholder may require the company to purchase their shares at fair value (as determined by binding arbitration, if the value is not agreed).

5.5 Disclosure by Shareholders in Publicly Traded Companies

Under the FMCA, a person is "*substantial product holder*" of a listed issuer if the person has "*relevant interest*" in 5% or more of the quoted voting products (eg, ordinary shares in a listed company) of the listed issuer. The definition of "*relevant interest*" for this purpose is broadly aligned with that set out in 4.5 Rules/Requirements Concerning Independence of Directors with regard to directors' interests in shares, although the two definitions diverge in some respects. The definition of "*relevant interest*" captures persons who are the ultimate beneficial owner of the share or who may exercise (or control the exercise of) the power to vote or the power to acquire or dispose of the share.

Persons are required to notify the listed issuer and the stock exchange when they become a substantial product holder, when the extent of their relevant interest changes (either up or down) by 1% or more of the total, or when they cease to be a substantial product holder.

In addition, a director or senior manager of a listed issuer who holds a relevant interest in quoted financial products of that listed issuer must disclose this to the listed issuer and the stock exchange.

Companies (whether listed or unlisted) that have 50 or more shareholders, 50 or more share parcels, and consolidated assets of NZD30 million or consolidated revenue of NZD15 million are also subject to the Takeovers Code (and, as such, are known as “Code companies”). The core requirement of the Takeovers Code is that no person may come to hold or control more than 20% of the voting rights in a Code company, or increase an existing holding or control above that proportion, except in specified ways – for example, by making a partial or full takeover offer to all shareholders or (for a holder of 50% to 90% of the voting rights) by increasing the holding by less than 5% per year.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Companies that carry out business in New Zealand are subject to varying financial reporting requirements that depend on their place of incorporation, ownership, size and listed or unlisted status, as follows.

- The following categories of company are required to file signed audited financial state-

ments with the Companies Office within five months of each balance date:

- (a) companies incorporated in New Zealand that are not subsidiaries of overseas companies and have assets greater than NZD66 million or revenue greater than NZD33 million in each of the preceding two financial years;
 - (b) overseas companies (and subsidiaries of overseas companies) that have assets greater than NZD22 million or revenue greater than NZD11 million in each of the preceding two financial years;
 - (c) companies with ten or more shareholders, unless they opt out by a 95% shareholder resolution; and
 - (d) any company where shareholders who together hold not less than 5% of the company’s voting shares have given notice requiring the company to opt in to these financial reporting requirements.
- The Listing Rules require listed companies to release annual reports (within three months of each balance date), which include audited financial statements and results announcements in relation to their full-year and half-year results.
 - Every issuer of a financial product that is regulated under the FMCA (ie, offerors of financial products for which “*product disclosure statement*”, akin to a prospectus, is required) is also required to file signed audited financial statements with the Companies Office within four months of each balance date – regardless of whether or not the issuer is listed (see **6.3 Companies Registry Filings**).

6.2 Disclosure of Corporate Governance Arrangements

If a company’s shareholders resolve to adopt, alter or revoke its constitution, the board is required to notify the Companies Office within

ten working days and include a copy of the constitution or amendments, which are then made publicly available. Other governing documents (eg, shareholders' agreements) do not have to be disclosed.

As regards corporate governance disclosures by listed companies, please refer to **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**. The Corporate Governance Code recommends that a listed issuer's code of ethics, board and committee charters, and certain policies (eg, concerning continuous disclosure, remuneration, diversity and financial product dealings) are made available on the issuer's website – together with any other key governance documents.

6.3 Companies Registry Filings

Companies are incorporated by registration with the Registrar of Companies. The Registrar is the head of the New Zealand Companies Office, which is a division of the Ministry of Business, Innovation and Employment. The following key filings are currently required to be made with the Companies Office and are publicly searchable on the Companies Office website:

- the company's constitution, registered office address, address for service of legal documents, and postal address;
- the name and addresses of the company's directors and its ten largest shareholders (or, if it is not a publicly listed company, all shareholders), as well as details of any change of directors;
- details of any shares issued by the company;
- details of the company's ultimate holding company (if any); and
- the annual return of the company.

The Companies Office has a wide range of powers to ensure that companies comply with their obligations under the Companies Act. For example, failure to provide the above-mentioned information within the timeframes specified by the Companies Act can result in fines for directors. In the case of failure to file an annual return, the Registrar can initiate action to remove the company from the New Zealand Companies Register. The Companies Office is also empowered to issue "*management banning orders*" that prohibit directors from managing companies. In the event of serious breaches, the Companies Office can prosecute the company or an individual. In support of these enforcement powers, the Companies Office also has powers to require production of relevant documents.

The Companies (Address Information) Amendment Bill passed its second reading on 19 February 2025. If enacted by Parliament, this Bill would allow a director to submit an application to the Registrar of Companies declaring that the public availability of their residential address is likely to result in physical or mental harm to them or a person residing with them, and to require an address for service to be used instead.

As mentioned in **6.1 Financial Reporting**, companies that have made one or more "*regulated offers*" under the FMCA must ensure the product disclosure statement and all other information relevant to the offer is filed on the Disclose Register, which is a publicly searchable electronic register operated by the Companies Office.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

For details of when a company's financial statements are required to be audited, please refer

to **6.1 Financial Reporting**. If they are required to be audited, this must be done by a qualified auditor or audit firm, in accordance with applicable auditing and assurance standards. For that purpose, the company must appoint an auditor at its annual meeting to hold office until the close of the next annual meeting. The auditor is automatically reappointed at each subsequent annual meeting unless they resign or cease to be qualified or the company passes a resolution to replace them.

A director or employee of the company (or a partner or employee of any such person) may not be appointed or act as an auditor of the company.

The directors must ensure that the auditor has access to the accounting records of the company at all times. The auditor may require a director or employee of the company to provide such information and explanations as the auditor thinks necessary for the performance of the auditor's duties. The directors must also ensure that the auditor is allowed to attend any shareholder meeting, receives all notices and other communications to shareholders regarding the meeting, and is permitted to speak at the meeting on any part of the business of the meeting that concerns the auditor.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

As noted in **4.8 Consequences and Enforcement of Breach of Directors' Duties**, the business and affairs of the company are required to be managed by – or under the direction or supervision of – the board. Directors must exercise the care, diligence and skill that a reasonable director would exercise (see **4.6 Legal Duties of Directors/Officers**). This requires directors to

keep themselves apprised of the business risks faced by the company.

The Corporate Governance Code recommends that:

- listed companies have a risk management framework (a summary of which should be included in the issuer's annual report);
- the board receives and reviews regular reports; and
- the issuer reports on the material risks – specifically, health and safety risks – facing the business and how these are being managed.

The Health and Safety at Work Act 2015 (the “HSW Act”) requires “*person conducting a business or undertaking*” (eg, a company) to ensure – as far as is reasonably practicable – the health and safety of all its workers while they are at work and that the health and safety of other persons is not put at risk from that work. The company and its directors can be found liable for breaches of the HSW Act, including where risks are not appropriately managed and systems are not set up to minimise risks.

For NZX-listed companies, the Listing Rules require disclosure of “*material information*” to the market immediately after a director or senior manager knew – or reasonably ought to have known – the information (unless an exception applies). This requires boards to have appropriate arrangements in place to ensure that any such information does in fact become known to a director or senior manager and can be released to the market as required.

NIGERIA

Law and Practice

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provides comprehensive advisory and transactional support in a wide range of practice areas, including regulatory, compliance and governance, commercial legal advisory, banking and finance, capital markets, public-private partnerships (PPP), real estate and infrastructure, litigation and dispute resolution, and intellectual property. The firm's lawyers are driven by a client-focused approach that combines technical excellence with commercial insight. Its commitment is to deliver legal solutions that are not only legally sound but also strategically aligned with our clients' business objectives.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

The Companies and Allied Matters Act (CAMA) 2020 is the primary legislation that governs the formation, registration, operation and regulation of businesses and corporate entities in Nigeria, and provides for the following principal forms of corporate/business organisations.

- Private company limited by shares (LTD): this structure is one of the most widely adopted forms of company registration in Nigeria, primarily because of its operational efficiency and uncomplicated nature. An LTD is a commercial entity established to conduct business for profit, and is a corporate entity separate from its owner(s) with perpetual succession, a common seal and the capacity to sue and be sued in its own name. The minimum share capital for private companies is NGN100,000, with the exception of companies with foreign participation, for which it is NGN100 million, and regulated entities with specific capital requirements. One of the key introductions of CAMA is the allowance of a single shareholder for private companies and a maximum is 50 members, excluding bona fide employees of the company.
- Public company limited by shares: a public company is a distinct legal entity that exists independently from its shareholders and owners and is capable of perpetual existence. Similar to a private company, a public company affords its shareholders limited liability, meaning that, in the event of the company's insolvency, the shareholders' losses are restricted to the amounts they initially invested, and they cannot be held personally liable for any debts incurred by the company. The minimum share capital for public companies is NGN2 million, with the exception of companies with foreign participation, for which it is NGN100 million, and regulated entities with specific capital requirements.
- Company limited by guarantee: an LTD/GTE company is one in which the liability of its members is restricted by the agreement of the amount that each member pledges to contribute to the assets of the company in the event that it is wound up. It is typically used to promote commerce, art, science, religion, sports, culture, education, research, charity or another similar object, and the company's income and property are to be applied solely to the promotion of its objects, with no portion paid to the company's members except as permitted by CAMA.
- Unlimited company: the defining feature of an unlimited company is that its members have unlimited liability so that, in the event of winding-up, members may be required to contribute without limit towards the company's debts and obligations. An unlimited company may be either private or public.
- Incorporated trustee: these are non-profit organisations formed by a group of persons united by a common interest in areas such as religion, sports, education or scientific development. These entities are not permitted to engage in business activities nor make profits for distribution.
- Limited liability partnership: an LLP is a business structure that combines the benefits of a partnership with that of a limited liability company. It must be formed by a minimum of two partners, for the purpose of carrying on a lawful business. In addition, there must be at least two designated partners, who must be individuals, with at least one resident in Nigeria. The designated partners are responsible for ensuring the LLP's compliance with appli-

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cable laws, and for the filing of the necessary documents, returns and statements.

- **Limited partnership:** this business structure consists of no more than 20 partners, including at least one general partner who has unlimited liability for the debts and obligations of the partnership, and at least one limited partner, whose liability is restricted to the amount contributed to the partnership. The general partners are responsible for the day-to-day management of the business, while limited partners typically do not take part in management.
- **Business name:** a business name is the simplest and most flexible form of business registration in Nigeria and is ideal for small-scale businesses and individual entrepreneurs. Under CAMA, a business name is not recognised as a separate legal entity, which means that the business and the owner are considered the same under the law, and the owner(s) bears personal liability for all business debts and obligations.

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance for companies in Nigeria are CAMA and the Nigerian Code of Corporate Governance 2018 (NCCG). The Code of Corporate Governance for Public Companies in Nigeria 2011, issued by the Securities and Exchange Commission (SEC), is applicable only to public companies. It is also important to note that there are industry-specific corporate governance codes issued by regulatory bodies such as the Central Bank of Nigeria (CBN), the National Insurance Commission (NAI-COM) and the Pension Commission (PENCOM), which provide tailored governance frameworks for organisations within their respective sectors.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with publicly traded shares are subject to the following requirements, among others.

- **Board composition:** the board of a publicly traded company should consist of no fewer than five members, with at least one independent non-executive director.
- **Interlocking directorship:** to preserve the objectivity and independence of the board, it is recommended that no more than two members of the same family should serve concurrently on the board of a public company. In addition, cross-membership on the boards of two or more companies should be discouraged.
- **Separation of power:** the positions of the chair of the board and chief executive officer in a publicly traded company must be separate and held by different individuals.
- **Board committees:** A public company is required to have audit, nomination, governance, remuneration and risk management committees.
- **Board evaluation:** to ensure continued effectiveness and accountability, the board of a public company is required to conduct an annual evaluation of its overall performance, as well as that of its committees, the chair and each individual director.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance Sustainability and Environmental, Social and Governance (ESG) Reporting

There is increasing regulatory focus on sustainability and ESG reporting in Nigeria. The Finan-

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cial Reporting Council of Nigeria (FRC) has continued to promote the adoption of sustainability disclosures in alignment with the IFRS Sustainability Disclosure Standards. In March 2024, the FRC released a Sustainability Reporting Roadmap, segmented into four distinct phases, as outlined below.

Phase 1 – early adopters

Entities that participated in this phase reported their sustainability-related information for the financial period that ended on or before 31 December 2023.

Phase 2 – voluntary adoption (2024–2027)

This phase covers accounting periods from 1 January 2024 to 31 December 2027. During this period, entities are expected to build internal capacity in preparation for mandatory adoption. Voluntary adopters are also required to undergo the Readiness Test Assessment before publishing any sustainability report.

Phase 3 – mandatory adoption

Public interest entities are expected to mandatorily adopt the IFRS Sustainability Disclosure Standards by 2028, while small and medium enterprises (SMEs) are expected to comply mandatorily by 2030.

Phase 4 – government and government organisations

Adoption will be considered following the finalisation of public sector sustainability standards by the International Public Sector Accounting Standards Board (IPSASB). A review will determine an appropriate commencement date for government entities.

Digital Governance and Cybersecurity Oversight

Boards are expected to play a more active role in overseeing digital transformation and managing cyber-risks. This includes establishing clear governance frameworks around data protection and IT resilience.

2.2 ESG Considerations

Materiality Assessment

Conducting a materiality assessment is a fundamental step in ESG reporting, as it enables companies to pinpoint the ESG issues that are most relevant to their operations, stakeholders and long-term value creation. This process helps organisations focus their reporting on areas that have the greatest impact on business performance and stakeholder expectations.

Standardised Reporting Framework

Companies are expected to adopt a globally recognised ESG reporting framework to ensure transparency and comparability in their disclosures. Nigeria has adopted the ISSB Standards, supported by the FRC's Sustainability Disclosure Roadmap, which offers a streamlined and consistent foundation for ESG reporting.

Governance Structure

Strong governance is the backbone of effective ESG reporting, requiring clearly defined structures that demonstrate active oversight by the board and senior management. Companies must disclose how ESG risks and opportunities are governed, including the roles and responsibilities assigned to leadership, the extent of board involvement in ESG oversight, and the accountability of management.

Data Collection

A key challenge for companies is the collection and management of accurate and verifiable

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ESG data. It is critical for companies to put clear processes in place for collecting and managing data, and ensuring that the data is reliable and consistent helps to build the trust of stakeholders and meets the expectations of regulators.

Areas of Focus

Corporate governance plays a critical role in today's corporate landscape, particularly in the formulation of succession policies within companies. Regulators now closely oversee the decision-making processes related to role transitions (see Section 11.2 of the NCCG).

A hot topic when it comes to corporate governance is the management of corporate finances. This constitutes a significant aspect of corporate governance, with public companies obliged to regularly disclose financial statements to uphold financial accountability.

Another emerging area of focus is the integration of ESG principles into corporate governance practices. This reflects a growing commitment among companies to address ESG concerns.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies and functions involved in the governance and management of a company are as follows.

- The board of directors is the governing body of a company, and is responsible for making key strategic decisions such as appointing and overseeing management, formulating corporate strategy, and monitoring risk, among others. The board operates independently of management and is expected to act

in the best interests of the company and its stakeholders, ensuring accountability, transparency and long-term sustainability.

- The executive management is responsible for the day-to-day operation of the company and for implementation of the company's strategy. Members are accountable to the board of directors and are expected to act in the best interest of the company and its stakeholders.
- Board committees support the board in achieving its goals and objectives by providing focused oversight and making informed recommendations to the board on relevant matters.
- The company secretary plays a key role in providing administrative and governance support to the board. The company secretary is responsible for offering advice and guidance on matters relating to company law, regulatory requirements, internal policies and corporate governance best practices. In addition, the company secretary ensures that the company remains compliant with all relevant laws and regulations, facilitates effective communication between the board and management, and manages essential duties such as organising board meetings, preparing minutes and maintaining statutory records.
- Regulators and government agencies oversee corporate activities, ensuring compliance and enforcing the implementation of laws, regulations and guidelines.

3.2 Decisions Made by Particular Bodies

Decision-making in companies takes place at various levels within the organisation, with each level having clearly defined roles and responsibilities. These decisions are made in accordance with relevant laws, as well as the company's internal policies and procedures, ensuring accountability, consistency and alignment with organisational goals.

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- As the owners of the company, shareholders have authority over certain matters that are exclusively within their purview. These typically include decisions such as an increase of share capital, a change of the company's name, making the liability of directors unlimited, sale of the company's major asset, voluntary winding-up of the company, declaration of dividend, etc. In addition, a company's Articles of Association may reserve other specific matters for shareholder approval, ensuring that key decisions reflect the interests of the ownership.
- The board of directors is responsible for making key strategic decisions that shape the direction of the company. These include matters such as capital investments, budget approvals, review and approval of financial statements, corporate governance oversight, long-term planning, risk management and the establishment of internal control systems. The scope of the board's authority may vary between organisations and is typically defined in the company's Board Charter, Delegation of Authority Policy, other internal governance documents, and applicable laws and regulations.
- The authority of board committees is defined by their respective Terms of Reference and delegated by the board.
- The authority of the executive management is subject to the authority delegated by the board of directors.
- Regulators and government agencies exert external influence on the management and governance of companies by enforcing the implementation of relevant laws and regulations, as well as issuing guidelines, circulars and directives to ensure compliance and promote best practices.

3.3 Decision-Making Processes

Company decisions are typically made through the passing of resolutions, which occur either at board meetings (by directors) or at general meetings (by shareholders). These resolutions are voted on in accordance with the provisions of CAMA and the company's Articles of Association. In situations where a formal meeting cannot be convened, or where the matter is urgent, a written resolution signed by all directors or members may be passed as a substitute for a physical meeting.

Decisions by regulators and government agencies are made internally based on their statutory powers and are subsequently published publicly – typically in the form of circulars, guidelines or directives – to inform and guide companies on compliance and governance expectations.

4. Directors and Officers

4.1 Board Structure

Regulatory governance frameworks in Nigeria provide for a unitary board structure, which typically consists of a mix of executive directors, non-executive directors and independent non-executive directors with the appropriate mix of knowledge, skills and expertise to effectively undertake the operations of the company.

4.2 Roles of Board Members

The roles and responsibilities of board members are typically outlined in the company's Board Charter, Articles of Association and governance policy. A general overview of these roles and responsibilities is provided below.

- The board chair is a non-executive director who provides leadership to the board and has the responsibility of ensuring board cohesive-

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ness and effectiveness, with the objective of supporting management in achieving corporate success. A key principle of Nigerian corporate governance is the separation of power: the chair of the board and the MD/CEO cannot be the same person. In addition, the chair of the board should not be a chair or member of any board committee.

- The MD/CEO is an executive director who oversees the day-to-day running of the company, including the implementation and achievement of the company's strategic objectives.
- Executive directors are senior management members involved in day-to-day operations, such as the chief financial officer (CFO), chief operating officer (COO), head of legal/company secretary, etc. They support the MD/CEO in achieving the company's goals.
- Non-executive directors oversee, constructively challenge and hold management accountable with respect to the implementation of strategy.
- Independent non-executive directors are non-executive directors with no ties to the company other than their board membership, ensuring an additional layer of objectivity.

4.3 Board Composition Requirements/Recommendations

To function effectively, a board requires the right mix of skills, experience and diversity. The composition of the board is influenced by external factors, such as the governance framework relevant to the sector in which the company operates, and by internal factors, including provisions in key company documents like the Shareholders Agreement, Articles of Association, Board Charter and governance policy. External factors typically include specific regulatory requirements, such as:

- board size;
- specific mix of executive, non-executive and independent non-executive directors;
- provisions for the prohibition of interlocking directorships; and
- the necessary board skills and expertise to oversee the business effectively.

Internal factors, on the other hand, are shaped by the company's own governance documents, which may set additional criteria for board composition based on the company's goals and structure.

The NCCG recommends that the board be of an adequate size relative to the scale and complexity of the company's operations. It emphasises the importance of considering factors such as the balance of knowledge, skills, experience, diversity and independence to ensure the board can objectively and effectively fulfil its governance duties and responsibilities.

The Code also advocates for the appropriate mix of executive, non-executive and independent non-executive directors, with the requirement that the majority of the board should be non-executive directors, to ensure a proper balance of oversight and management. The Code also highlights the need for a sufficient number of members who are qualified to serve on the board's various committees and who can form a quorum at board meetings.

4.4 Appointment and Removal of Directors/Officers

The first directors of a company are appointed at incorporation by the promoters of the company, while subsequent appointment is by ordinary resolution of shareholders at the general meeting. However, where there is a casual vacancy arising from the death, retirement, resignation or

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removal of a director, the board of directors may appoint a new director to fill the vacancy and present such appointment to the shareholders at the next general meeting for ratification.

The following persons are disqualified from being directors under the Nigerian law:

- a child (ie, a person under the age of 18 years);
- a person of unsound mind;
- a person suspended or removed;
- a person disqualified owing to insolvency, fraudulent activities, bankruptcy or unsound mind; and
- a corporation other than its representative appointed to the board for a given term.

Unless otherwise provided in the company's Articles of Association, at the first annual general meeting (AGM) of the company all the directors are to retire from office, and one-third of the directors - or, if their number is not three or a multiple of three, then the number nearest one-third - shall retire from office at the AGM in every subsequent year. The directors to retire in every year are those who have been longest in office since their last election; however, between persons who became directors on the same day, those to retire are determined by lot (unless they agree among themselves). Directors retiring by rotation can be reappointed by shareholders.

The process and criteria for the appointment and removal of directors would typically be contained in the Board Charter or policy on board appointment, with oversight delegated to the committee responsible for governance and nominations.

Unless provided in the Articles of Association or Board Charter, the removal of a director is

a statutory process and thus the provisions of CAMA would be applicable as follows.

- The person(s) wishing to remove the director will issue a notice of the resolution to the company at least 28 days before the date of the meeting.
- Upon receiving the notice, the company secretary will:
 - (a) send a copy to the director sought to be removed; and
 - (b) issue notice of the meeting at least 21 days before the meeting date, along with any representations made by the director.
- At the meeting, the director sought to be removed will be allowed to present their case and read their representations to the members if they were received late or not received at all due to the company's fault.
- Following the representation by the director, the company shall now pass an ordinary resolution to remove the director and authorise the secretary to file Form CAC 7A – Notice of vacation of office/removal of director within 14 days of removal with the Corporate Affairs Commission (CAC).
- Record the removal in the register of directors and the register of directors' residential addresses and, if necessary, amend the register of directors' shareholding.

4.5 Rules/Requirements Concerning Independence of Directors

CAMA and the NCCG have set rules to ensure the independence of directors. The Business Facilitation Act stipulates that one-third of the board composition should be independent non-executive directors. The NCCG provides that an independent non-executive director must not possess a shareholding in the company the value of which is material to them such as to impair their independence or in excess of 0.01%

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of the paid-up capital of the company. Although Section 275 (1) of CAMA sets a threshold of not more than 30% equity holding in the company to determine the independence of an independent non-executive director of a public company, companies typically apply the provision of the NCCG in setting the criterion of independence for their independent non-executive directors.

Directors are expected to disclose any form of conflict of interest or potential conflict of interest in the company they serve as director, as recommended by the NCCG. Conflicts of interest include insider dealing, a personal interest in transactions with the company, and familiar relationships.

4.6 Legal Duties of Directors/Officers

The duties of the directors of a company extend to the officers of the company and are statutorily outlined. These duties include:

- a duty to always act in what the director believes to be in the best interests of the company, in good faith, to preserve the company's assets, further its business and promote the purposes of the company;
- a duty to further the company's business and purposes in a faithful, diligent and careful manner – in doing so, the director must pay attention to what an ordinarily skilful director would do in those circumstances and must also have regard to the impact of the company's operations on the environment;
- a duty to always take into consideration the interests of the company's employees, as well as the interests of its members;
- the duty of a director to exercise powers as a director based on the specified obligations within their role and not to do so for a collateral purpose;

- a duty not to fetter discretion to vote in a particular way (the director is expected to use their voting power and discretion in the best interest of the company);
- where a director is allowed to delegate powers under any provision of CAMA, such director must not delegate the power in a way that may amount to an abdication of duty;
- a duty to ensure that the director's interest does not conflict with any of the director's duties to the company; and
- a duty not to make unnecessary secret profit while managing and utilising the properties of the company as a director - if such profit is made, the director is expected to account for it.

4.7 Responsibility/Accountability of Directors

The directors' statutory duties under CAMA are designed to serve the best interests of the company. These duties are fiduciary in nature, meaning directors must act in good faith and prioritise the company's interests above their own. They must avoid any actions that would violate this duty. Directors are also expected to exercise their powers for proper purposes and to do so with care, skill and diligence.

Directors are required to consider the interests of the company's employees as well as its members (shareholders) when performing their duties. However, where directors act in good faith and in pursuit of the company's objectives and interests in the course of fulfilling their duties to the company, they will not be held liable for any adverse effects their actions may have on a member or employee.

Therefore, while directors are encouraged to take the interests of employees and members into account, it is clear that the ultimate priority

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remains the best interest of the company itself. Directors are primarily obliged to act in a manner that promotes the success and sustainability of the company as a separate legal entity, even if such actions may, in some instances, negatively impact certain stakeholders.

4.8 Consequences and Enforcement of Breach of Directors' Duties

As a general rule, a company - rather than its shareholders - can bring a claim against one of its directors for breach of duty, given that the duty is owed by the directors to the company itself. The options available to the company include order of injunction, compensation for damages, and revocation of contract. However, there are instances that entitle a shareholder to enforce a breach of director's duties, including:

- entering into illegal or ultra vires transactions;
- purporting to do by ordinary resolution any act that is required by CAMA or the company's articles/charter to be done by special resolution;
- any act or omission affecting the shareholder's individual rights as a member of the company;
- committing fraud on either the company or its minority shareholders;
- where a company meeting cannot be called in time to be of practical use in redressing a wrong done to the company or to its minority shareholders; and
- where the directors are likely to derive a profit or benefit - or have profited - from their negligence or from their breach of duty.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other bases for claims or enforcement against directors or officers for breaches of corporate

governance requirements in Nigeria are as follows.

- **Statutory regulations** – Nigerian companies are subject to various statutory regulations and regulatory bodies, such as the SEC and the CAC. Directors and officers must comply with these regulations; failure to do so can result in enforcement actions.
- **Common law** – directors can be held liable under common law principles for actions such as negligence, breach of duty of care, or breach of trust.
- **Shareholder actions** – shareholders in Nigerian companies have the right to bring actions against directors for breaches of duty or other misconduct through derivative actions or direct claims.
- **Criminal offences** – directors and officers can also face criminal liability for offences such as fraud, insider trading, or other financial crimes under Nigerian criminal law.
- **Tort law** – directors can be sued under tort law for actions such as defamation, negligence or misrepresentation.
- **Regulatory enforcement** – regulatory bodies such as the Nigerian Stock Exchange (NGX) or the FRC have powers to enforce compliance with corporate governance standards, and can take enforcement actions against directors and officers for non-compliance.

The liability of a director is generally limited. A director will not be held personally liable for actions taken in the ordinary course of business, provided such actions are carried out in good faith and in the best interest of the company. However, directors may be personally liable in certain circumstances, particularly where their conduct involves wrongdoing. In such cases, the law lifts the veil of protection usually afforded to

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directors, holding them personally accountable for their misconduct.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The remuneration of non-executive directors is determined by the company at its general meetings. Typically, the board proposes the remuneration package to shareholders based on the recommendation of the committee responsible for nomination, governance and remuneration. In making such recommendations, factors such as industry standards, the expected time commitment and the company's financial capacity are considered. The components of non-executive directors' remuneration generally include directors' fees and sitting allowances, which are required to be disclosed in the company's annual report. Notably, non-executive directors are prohibited from receiving performance-based compensation.

The remuneration components of executive directors who are also employees of the company are typically outlined in their letters of employment. Such remuneration usually includes benefits such as an annual salary, healthcare, car allowance, housing allowance, travel allowance, telephone allowance and other performance-based compensation. These benefits are subject to board approval and must be disclosed to shareholders. Executive directors, unlike non-executive directors, are not entitled to receive sitting allowances or directors' fees.

Failure to comply with the approval process would render the activities of the board void.

4.11 Disclosure of Payments to Directors/Officers

Under the NCCG, a company's remuneration policy as well as the remunerations of all directors are required to be disclosed in the company's annual report. Companies are also advised to implement a claw-back policy to recover excess or undeserved rewards (eg, bonuses, incentives, share of profits, stock options, or any performance-based reward) from directors and senior employees.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

A shareholder's relationship with the company in which they hold shares is a contractual one. The relationship between the shareholders and the company is guided by the Shareholders Agreement, Memorandum And Articles Of Association to the same extent as if they were covenants on the part of the company, and each member must observe the provisions.

The shares held by the members give a right of participation in the company. A shareholder does not have a proprietary interest in the underlying assets of a company; however, they are entitled to a share of the distributed profits of the company in proportion to their respective shareholdings and, on a winding-up, to the surplus assets of the company after the company's creditors have been repaid in full.

Shareholders are not liable for the acts of the company, except in very limited circumstances when the corporate veil can be pierced, where a company's limited liability status is set aside, and a shareholder is liable for the company's acts.

Information regarding a company's shareholders and their shareholding records can be obtained through the company's profile on the CAC portal.

5.2 Role of Shareholders in Company Management

Shareholders are generally not involved in the day-to-day operations of the company. This responsibility lies with the board of directors, as provided by law and outlined in the company's Articles of Association. However, certain matters are reserved for shareholder approval, including:

- the appointment and removal of directors;
- the determination of directors' remuneration;
- the appointment of auditors and approval of their remuneration;
- alteration of the company's share capital;
- alteration of the Memorandum and Articles of Association of the company;
- approval of 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 of the company's name;
- making the liability of directors unlimited;
- the appointment of a person over 70 years of age as a director in a public company;
- the sale or transfer of the company's major asset;
- the winding-up of the company;
- an application to strike off the company's name from CAC's register; and
- declaration of dividends.

Shareholders make decisions by way of resolutions passed during general meetings. However, CAMA allows private companies to pass written resolutions without holding a meeting, provided the written resolution is signed by all shareholders.

5.3 Shareholder Meetings

CAMA requires shareholders to hold two types of meetings: the statutory meeting and the AGM. A statutory meeting must be held within six months of the company's incorporation and is mandatory only for public companies. The AGM, on the other hand, is required to be held annually by all companies, unless exempted by law.

Every company, except a small company or a company with a single shareholder, is required to hold an AGM each year, and no more than 15 months shall elapse between the date of one AGM and the next. The CAC has the power to grant an extension for holding the AGM, but such extension cannot exceed three months. Notice for the AGM must be sent to the shareholders at least 21 days prior to the meeting. However, a shorter notice may be sent if all shareholders entitled to attend and vote at the meeting consent to it.

CAMA provides that all statutory and annual general meetings must be held in Nigeria; however, these meetings may be held electronically if they are conducted in accordance with the company's Articles of Association.

Two types of business can be transacted during an AGM: ordinary business and special business. Ordinary business includes the declaration of dividends, presentation of the financial statements, reports of the directors and auditors, the election of directors in the place of those retiring, fixing of the remuneration of the auditors, and the removal and election of auditors and directors, while special business is any business other than ordinary business.

At any general meeting, a resolution put to the vote is decided by a show of hands, unless a poll is demanded by the chair or at least three mem-

bers present in person or by proxy or a member or members representing at least one tenth of the total voting rights of all the members having the right to vote at the meeting.

5.4 Shareholder Claims

As a general rule, only a company can bring a claim against any form of breach committed against it by its directors. However, shareholders may bring a claim on behalf of the company against the company and the directors under the following instances:

- entering into any transaction that is illegal or ultra vires;
- fraud against either the company or the minority shareholders where the directors fail to take appropriate action to redress the wrong done;
- where a company meeting cannot be called in time to be of practical use in redressing a wrong done to the company or to minority shareholders;
- purporting to do by ordinary resolution any act that by its articles or this act is required to be done by special resolution;
- any act or omission affecting the applicant's individual rights as a member;
- where the directors are likely to derive a profit or benefit – or have profited or benefitted – from their negligence or their breach of duty; and
- any act or omission where the interest of justice so demands.

Shareholders may bring an action in court through a member's direct action, personal or representative action, or derivative action.

5.5 Disclosure by Shareholders in Publicly Traded Companies

In publicly traded companies, shareholders are required to disclose their shareholding interests when they acquire a significant percentage of the company's shares. Under Nigerian law, particularly in accordance with the Investments and Securities Act and relevant SEC regulations, any person who acquires 5% or more of a company's voting shares must notify the company and the SEC within a prescribed period, typically within ten business days.

Shareholders are also obliged to disclose any substantial changes in their shareholding, such as further acquisitions or disposals that alter their percentage of ownership. The company, in turn, must notify the relevant securities exchange and update its records. This disclosure framework promotes transparency, prevents insider trading and ensures that investors and regulators are kept informed about significant changes in the ownership structure of listed companies.

The Persons of Significant Control Regulation is applicable to all companies, and requires a person with significant control (PSC) in a company to disclose to the company the particulars of such control within seven days of acquiring such significant control. Companies must, in turn, notify the CAC within one month of receipt of the information, disclose the information in their annual returns to the CAC, and update their registers of members with the appropriate details. Significant control arises where a natural person owns or controls at least 5% of the company's shareholding.

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6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

In Nigeria, companies are subject to various annual and periodic financial reporting obligations to ensure regulatory compliance and promote transparency. These requirements apply generally to all companies, with additional sector-specific obligations imposed by various regulatory bodies, depending on the nature of the company's operations.

The key financial reporting obligations are as follows.

- Under CAMA, all companies are required to prepare and file their annual financial statements with the CAC, within 42 days after the annual general meeting.
- Publicly quoted companies are required to file annual financial statements, quarterly reports and corporate governance reports with the NGX.
- Public companies (both quoted and unquoted) are required to submit their annual financial statements, quarterly reports and corporate governance reports to the SEC.
- Public interest entities are required to file their annual financial statements and corporate governance reports with the FRC.
- Insurance companies are mandated to file their annual financial statements with the National Insurance Commission (NAICOM).
- Banks and other financial institutions are required to file their annual financial statements and quarterly reports with the CBN.
- Banks, insurance companies and deposit, provident or benefit societies are required to file a Statement of Affairs (Fourteenth Schedule) with the CAC on the first Monday of February and the first Tuesday of August each year.

6.2 Disclosure of Corporate Governance Arrangements

Companies are required to disclose the extent of their compliance with the NCCG on an annual basis, outlining the nature of the company's compliance and, where applicable, explaining any areas of non-compliance. The report must be filed on the FRC's portal on or before March 31st each year and, for publicly listed companies, must also be filed with the NGX on or before March 31st annually. In addition, public companies are required to submit an annual corporate governance report in compliance with the SEC Corporate Governance Guidelines on or before January 31st.

6.3 Companies Registry Filings

The CAC is the regulatory body responsible for incorporating companies in Nigeria. Companies are required to make various filings with the CAC, as needed, including:

- annual returns;
- notice of appointment/change of director;
- notice of share increase;
- notice of appointment/change of company secretary;
- notice of appointment/change of external auditors;
- notice of transfer of shares;
- allotment of shares;
- alteration of Memorandum;
- Statement of Affairs (Fourteenth Schedule);
- notice of change of registered address;
- notice of change of persons with significant control; and
- notice of resolution to wind up.

The filings must be made within specific timeframes, and failure to comply can result in penalties, which may be a one-off payment or daily penalties, depending on the nature of the filing.

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Failure to file annual returns for a continuous period of ten years may result in the company being struck off the register, effectively leading to its dissolution. These filings are available at the CAC and can be inspected for a fee. Please note that the list above is not exhaustive.

The CAC has various supervisory powers over entities, including the authority to:

- regulate and monitor the registration and operation of companies, business names and incorporated trustees;
- inspect company records; and
- investigate suspected breaches of CAMA, impose penalties for non-compliance and, where necessary, strike off defaulting entities from the register.

Through these supervisory functions, the CAC plays a critical role in promoting good corporate governance and legal compliance among registered entities.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

In line with CAMA, every company – except a small company as defined under Section 394 (3) of CAMA or a company that has not carried out business since its incorporation – is mandated to appoint an external auditor to audit its financial statements.

One of the key requirements governing the relationship between the company and the auditor is independence. An auditor is not expected to serve a company for more than ten consecutive years and must observe a seven-year cooling-off period before potential reappointment. To further preserve independence, there should be a rota-

tion of the audit engagement partner every five years. Also, it is expected that a cooling off period is observed before the company can employ any member of the audit team.

Companies are expected to establish policies on the appointment and independence of auditors, and on the scope of non-audit work an external auditor can undertake.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The NCCG places the responsibility for risk management and internal controls squarely on the board of directors. The board is required to ensure the establishment of a robust and comprehensive risk management framework that identifies, assesses and mitigates risks. This framework must be effectively integrated into the company's day-to-day operations and clearly communicated across all levels of the organisation in simple and practical terms. In addition, the board must ensure that sound internal control mechanisms, policies and procedures are in place, and that they are regularly reviewed and updated to address evolving risks.

Oversight of these functions is typically exercised through the board's audit and risk management committee, which is also responsible for ensuring that the internal audit charter clearly outlines the roles, duties and responsibilities of the internal audit function. It must ensure that the individual or firm performing the internal audit function – whether internal staff or an outsourced firm – is properly qualified and operates in full compliance with the charter and applicable professional standards. These measures are essential to safeguard shareholders' interests and ensure the company's long-term sustainability.

Trends and Developments

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Jackson, Etti & Edu

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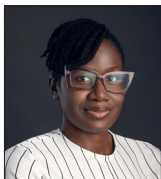


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Integrating ESG into Corporate Governance in Nigeria

Environmental, social and governance (ESG) reporting refers to how companies score on these responsibility metrics and standards for potential investments. Environmental criteria gauge how a company safeguards the environment; social criteria examine how it manages relationships with employees, suppliers, customers and communities; and governance measures a company's leadership, executive pay, audits, internal controls and shareholder rights.

Historically, ESG became a household name in the corporate governance space after its first mainstream appearance in a UN-commissioned report titled *"Who Cares Wins"*. Throughout the years, this report has evolved to be integral in the corporate governance practice of corporations, especially public companies. It is now important for companies to position themselves to attract the right investors by incorporating and maintaining high compliance with the principles of ESG.

This article focuses on governance, and lays more emphasis on the evolving landscape of corporate governance, with a specific spotlight on the integration of ESG principles. During the past decade, there has been a notable shift in corporate governance practices towards incorporating ESG considerations. This article provides insight into the reasons behind such a shift, the challenges and opportunities it presents, and the potential impact on corporate behaviour and performance. It highlights the growing importance of ESG in shaping corporate governance frameworks and offers insights into best practices for organisations seeking to adopt and effectively implement ESG principles.

What is corporate governance?

Corporate governance is the system of rules, practices and processes by which a company is directed and controlled. Corporate governance essentially involves balancing the interests of a company's stakeholders, which can include shareholders, senior management, customers, suppliers, lenders, the government and the community. As such, corporate governance encompasses practically every sphere of management, from action plans and internal controls to performance measurement and corporate disclosure.

Corporate governance serves as the foundation for effective decision-making, risk management and accountability within organisations. Traditionally, governance frameworks focused primarily on financial performance and compliance with regulatory requirements. The Nigeria Code of Corporate governance (NCCG) 2018 incorporates corporate governance in corporations by recommending and mandating an annual Corporate Governance Evaluation Report filing (Principle 15 of the NCCG).

However, in recent years, there has been a paradigm shift towards a more holistic approach that considers the broader impact of corporate activities on stakeholders and society at large. This shift has been driven by various factors, including increasing stakeholder expectations, regulatory pressures and the recognition of the interconnectedness between business success and ESG factors.

Evolution of ESG in corporate governance

In Nigeria, ESG has transformed from a mere buzzword for corporates into the adoption of core principles and practices. In other words, the integration of ESG principles into corporate governance practices has been a gradual but significant process. Initially, ESG considerations were

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often viewed as separate from core governance functions (somewhat peripheral to the operations of the company) - relegated to specialised sustainability or Corporate Social Responsibility (CSR) departments - and their impact was under-emphasised. However, as awareness of ESG risks and opportunities has grown, there has been an integration between ESG and corporate governance, facilitated by the recognition that ESG factors can have material impacts on business performance, reputation and long-term sustainability.

The evolution of ESG factors within the realm of corporate governance represents a transformative journey from traditional governance paradigms towards a more holistic and sustainable approach to decision-making and accountability. This evolution has been shaped by various catalysts and milestones, reflecting a growing recognition of the interconnectedness between corporate behaviour, societal impacts and long-term value creation.

Emergence of sustainability discourse

The increased conversation around sustainable discourse has led to the inevitable growth of ESG in Nigeria. Corporations now have the responsibility of thinking long-term while taking into consideration issues such as the availability of basic life-sustainable goods, raising the standard of living, and general service offering. The call for broader societal impacts, especially in an oil-producing country such as Nigeria, will enable companies to place priority on innovation that is environmentally friendly and sustainable.

Rise of CSR

CSR is a self-regulating business model that helps a company be socially accountable to itself, its stakeholders and the public. The concept of CSR gained prominence as companies

recognised the importance of not only maximising shareholder value but also considering the interests of various stakeholders, including employees, communities and the environment. Most importantly, CSR concentrates on the voluntary actions made by businesses to solve societal issues with initiative. CSR became a means for companies to demonstrate their commitment to ethical practices and sustainability.

Improved stakeholder capitalism

Stakeholder capitalism proposes that corporations should serve the interests of all their stakeholders and not just shareholders. Stakeholders can include investors, owners, employees, vendors, customers and the public at large. A shift from the traditional shareholder-centric model of governance gradually gave way to a more inclusive approach known as stakeholder capitalism. This shift emphasised the importance of balancing the interests of shareholders with those of other stakeholders, such as employees, customers, suppliers and society at large. ESG considerations became central to this redefined understanding of corporate purpose and responsibility.

Regulatory framework

The NCCG administered by the Financial Reporting Council of Nigeria (FRC) now makes it a requirement to maintain a policy document that promotes the intra- and interpersonal relationships of the company and other stakeholders. This requirement is aimed at enhancing transparency and accountability regarding companies' environmental and social impacts. These regulatory developments provide further impetus for organisations to integrate ESG considerations into their governance frameworks.

NIGERIA TRENDS AND DEVELOPMENTS

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Rise of sustainable investing

The rise of sustainable investing and Socially Responsible Investment (SRI) funds signalled a significant shift in investor preferences. Institutional investors, asset managers and pension funds increasingly considered ESG criteria in their investment decisions, driving demand for ESG-aligned companies and putting pressure on corporations to improve their ESG performance.

Integration into governance frameworks

ESG factors gradually came to be recognised as material considerations for corporate governance. Boards of directors began to incorporate ESG oversight into their responsibilities, recognising the importance of identifying and managing ESG risks and opportunities. Corporate governance codes and guidelines started to explicitly reference the need for boards to consider ESG issues in their decision-making processes.

Mainstream acceptance and integration

In recent years, ESG integration has moved from the fringes to the mainstream of corporate governance practices. Companies across industries and geographies have embraced ESG principles as integral components of their governance frameworks. ESG metrics are now routinely included in corporate reporting, annual meetings and board discussions, reflecting a fundamental shift in how organisations approach sustainability and responsible business conduct.

In Nigeria, the FRC has taken active steps to promote the adoption of sustainability disclosures in line with the IFRS Sustainability Disclosure Standards. In March 2024, the FRC released a Sustainability Reporting Roadmap, which outlines a phased approach. Under this roadmap, Public Interest Entities are expected to mandatorily adopt the IFRS Sustainability Disclosure

Standards by 2028, while Small and Medium Enterprises (SMEs) are expected to comply by 2030. This development signals a growing regulatory expectation for companies to embed sustainability and transparency into their long-term strategic planning and reporting obligations.

Continued evolution and challenges

The evolution of ESG in corporate governance is an ongoing process, marked by continued refinement of practices and standards. While significant progress has been made, challenges remain, including the need for standardised ESG reporting frameworks, robust data collection and verification mechanisms, and greater board diversity and expertise in sustainability matters. Addressing these challenges will be crucial for further advancing the integration of ESG principles into corporate governance and ensuring that businesses continue to uphold their commitment to sustainability and long-term value creation.

In summary, the evolution of ESG in corporate governance represents a fundamental shift towards a more inclusive, responsible and sustainable approach to business management and decision-making. From its roots in sustainability discourse to its mainstream acceptance today, the journey of ESG integration reflects a growing recognition of the importance of considering ESG factors in corporate governance frameworks.

Drivers of ESG integration

Several factors have contributed to the increasing integration of ESG principles into corporate governance, as follows.

- Stakeholder expectations - these are one of the key drivers of ESG in corporate governance. Investors, consumers, employees

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and other stakeholders are placing greater emphasis on sustainability, ethical business practices and social responsibility. Companies that fail to address these expectations risk reputational damage and loss of trust, as well as investment.

- Regulatory pressures/framework - one of the key drivers of improved ESG in corporate governance is the regulatory framework, which regulators are steadily evolving to address ESG issues. This framework mandates companies to provide greater transparency concerning their environmental and social performance. Non-compliance with these regulations may attract sanctions from the regulator.
- Financial materiality - growing evidence suggests that ESG factors can materially impact financial performance and risk management. Investors are increasingly factoring ESG criteria into their investment decisions, driving demand for ESG-aligned companies.
- Long-term value creation - incorporating ESG considerations into governance frameworks is seen as being essential for long-term value creation and resilience. Companies that effectively manage ESG risks and opportunities are better positioned to adapt to evolving market dynamics and stakeholder expectations.

Challenges and opportunities

The implementation of ESG principles in corporate governance has its unique challenges, especially in Nigeria. The following list discusses these challenges and opportunities in the intersection of ESG with corporate governance.

- Data availability and quality - in this part of the world (where data collection, availability and quality are already challenging), obtaining reliable ESG data can be difficult, particularly for non-financial metrics. Companies may struggle to collect, standardise and disclose relevant data consistently and comparably. Therefore, it becomes a challenge to measure the progress of an organisation's ESG compliance.
- Stakeholder engagement - communication is a critical vehicle in corporate governance, and the NCCG expects companies to maintain a communication policy. Effective stakeholder engagement is crucial for identifying material ESG issues, setting priorities and implementing strategies. Companies must establish robust mechanisms for dialogue and collaboration with stakeholders.
- Board oversight and expertise - it is acknowledged that ESG is an evolving philosophy in Nigeria, requiring ongoing training and awareness efforts to achieve a commendable level of proficiency among board members. Although boards hold a crucial responsibility in supervising ESG integration endeavours, there is often a shortage of expertise in sustainability-related domains. Therefore, enhancing both board diversity and competence becomes imperative for ensuring effective ESG governance.
- Integration into decision-making - embedding ESG considerations into core business processes and decision-making frameworks requires a cultural shift within organisations. Companies must align incentives, metrics and performance targets to promote ESG integration.
- Prospects of enhanced risk management - ESG data is essential for assisting businesses in engaging in effective risk management because it enables them to plan for compliance, enhance voluntary disclosures and develop risk mitigation roadmaps to handle threats in advance. By identifying and addressing ESG risks, companies can

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mitigate potential financial, operational and reputational impacts.

- Improved stakeholder relations - as stated earlier, ESG in corporate governance is pro-stakeholder in theory, and demonstrating a commitment to ESG principles can enhance trust and credibility with stakeholders, leading to stronger relationships and increased loyalty.
- Innovation and competitive advantage - embracing sustainability can drive innovation, efficiency and differentiation, positioning companies for long-term success in a rapidly changing market.
- Access to capital/investment - ESG-aligned companies may benefit from lower financing costs, increased access to capital and enhanced investor confidence, particularly as sustainable investing continues to gain momentum.

Recommendations

Impressively, corporates have outlined best practices for the integration of ESG in corporate governance. To effectively integrate ESG principles into corporate governance, organisations can adopt the following best practices.

- Board leadership and oversight - the board leadership is expected to offer decisive guidance on ESG matters, set up supervisory frameworks and incorporate sustainability into board structure and committees. Board leadership should actively seek to augment their understanding of ESG through training sessions and workshops. This aspect should also factor into the company's annual board evaluation as a measurable criterion.

- Stakeholder engagement - engage with a diverse range of stakeholders to understand their perspectives, concerns and expectations regarding ESG performance.
- Robust risk management - conduct regular ESG risk assessments, identify material issues and develop strategies to mitigate risks and capitalise on opportunities.
- Transparency and disclosure - provide comprehensive and transparent disclosure on ESG performance, policies and practices, using standardised frameworks.
- Integration into strategy and operations - integrate ESG considerations into strategic planning, investment decisions, product development, supply chain management and other core business processes.

Conclusion

The integration of ESG principles into corporate governance is a continuous process that represents a fundamental shift in how organisations approach sustainability, ethics and long-term value creation, from shareholder theory to stakeholder theory. While challenges remain, the benefits of ESG integration are clear: enhanced risk management, improved stakeholder relations, innovation, and access to capital/investment. By embracing ESG principles and implementing best practices, companies can strengthen their governance frameworks, drive sustainable growth and contribute to a more resilient and inclusive global economy. Organisations are encouraged to align with the global best practice in implementing ESG rules in corporate governance.

PORTUGAL



Law and Practice

Contributed by:

Susana Braz, Jaime Costa and Tomás Simões

Santiago Mediano e Associados, SP, RL

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Santiago Mediano e Associados, SP, RL was founded in 2003. The firm combines business-oriented advice with strong legal foundations. The corporate department team advises clients on corporate matters in cross-border transactions, governance and mergers and acquisitions, negotiating deals at the national and international level, including the corresponding due diligence procedures when required. The team, consisting of five professionals in this area, supports clients in all aspects of their business and corporate activities and related areas such as

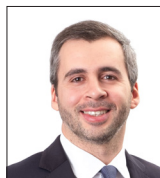
real estate, working in close co-ordination with the firm's other teams. With offices in Lisbon and Madrid, the firm is committed to assisting its clients in finding solutions to all their legal needs. Recent works include advising a Spanish company on the planning and structuring of a corporate transaction in Portugal, and assisting a leading waste management conglomerate with an acquisition by carrying out legal due diligence and advising on the respective sale and purchase agreement.

Authors



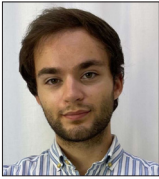
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Santiago Mediano e Associados

1. Introductory

1.1 Forms of Corporate/Business Organisations

General Characteristics of the Principal Forms of Corporate Organisations

Private limited company (Sociedade por quotas or Lda), equivalent to the French SARL or to the German GmbH

- This type of company is particularly suited to small and medium-sized enterprises.
- A minimum share capital is not required.
- Each quota must have a minimum value of EUR1.00.
- A minimum of two shareholders is required.
- Shareholders are liable under the terms of the by-laws and only up to the amount of the company's share capital. Only the company's assets are liable towards third-party creditors.
- The managers bear subsidiary liability towards third parties and share joint liability between them for all taxes related to the company's financial year, unless they are able to prove that the insufficiency of the company's assets to cover tax liabilities was not due to any fault on their part.

Public limited company (Sociedade Anónima or S.A.), equivalent to the French SA or to the German AG

- This type of company is particularly suited to larger enterprises, as it entails a more complex administrative structure.
- It requires a minimum share capital of EUR50,000;
- Each share must have a nominal value equal to or higher than EUR0.01;
- The minimum number of shareholders to incorporate a company is five. However, single-shareholder companies are permitted, provided the sole shareholder is a corporate entity.

- Shareholders are liable only up to the amount of the shares they hold.
- The directors bear subsidiary liability towards third parties and share joint liability between them for all taxes related to the company's financial year, unless they are able to prove that the insufficiency of the company's assets to cover tax liabilities was not due to any fault on their part.

Sole proprietorship – Sociedade Unipessoal Por Quotas (Unipessoal, Lda./Limitada)

- It has essentially the same structure as the private limited company.
- It is composed of one shareholder – an individual or a company.
- It cannot have as a shareholder another sole proprietorship.
- An individual cannot be a shareholder of more than one sole proprietorship.
- The sole shareholder has the same responsibilities as the general meeting of shareholders;
- The name of these companies must include the expression “Unipessoal” (sole proprietor).

Comparing the Types of Companies

The main advantages of a public limited company lie, in the ease with which its shares can be transferred, the ability to raise capital through public subscription, and, to some extent, the ability to keep the identities of shareholders confidential. This type of company also tends to project the image of being larger and more robust. However, such companies come with a more complex organisational structure and, as a result, are more costly to operate than a private limited company, since they are subject to stricter requirements and formalities.

On the other hand, private limited companies offer a simpler, more flexible structure, making

them an excellent choice for private, closely held companies where shareholder changes are infrequent and anonymity is not a primary concern.

In any event, under Portuguese law, it is possible to convert a company from one type to another, provided that all legal conditions are fulfilled and there is nothing in the company's by-laws prohibiting such a transformation.

1.2 Sources of Corporate Governance Requirements

Main Sources

The principal sources of corporate governance requirements for companies in Portugal are the Companies Code (*Código das Sociedades Comerciais* or CSC) and the Portuguese Securities Code (*Código dos Valores Mobiliários* or CVM).

There are, however, specific provisions for:

- **Listed Financial Institutions:** The recommendations issued by the Portuguese Central Bank (BdP) play a central supervisory role in overseeing the governance models adopted by these institutions. Institutions must periodically evaluate their governance model to identify opportunities for improvement and must take the necessary measures to correct any detected deficiencies. In the exercise of supervision, and adhering to the principle of proportionality, the Bank of Portugal maintains regular contact with the members of the governing bodies of the institutions it supervises. If deemed necessary, it may attend the meetings of these bodies in person.
- **Public Interest Entities:** The legal regime applicable to public companies (*Regime Jurídico do Setor Público Empresarial* or RJSPE) sets out rules for the formation, organisation, and governance of public companies, as well as for the exercise of powers

inherent to the ownership of shareholdings which aim to ensure efficiency, transparency, and accountability in the management of public companies.

- **Public Limited Sports Companies (*Sociedades Anónimas Desportivas* or SADs):** The corporate governance of Portuguese SADs is set out by Law 39/2023 of 4 August 2023, which promotes transparency in the management of SADs by setting out, among others, the obligation to disclose annually to the organising sports bodies the identity of the members of the management body. The Portuguese Institute of Sports and Youth (*Instituto Português do Desporto e Juventude* or IPDJ) is the supervisory entity responsible for verifying the suitability and any potential conflicts of interest of qualified investors, directors, and managers.

Soft Law

Further, the Securities Market Commission (*Comissão do Mercado de Valores Mobiliários* or CMVM) has been issuing recommendations on corporate governance since 1999, which initially only applied to listed companies, and that have been compiled in the Corporate Governance Code (*Código de Governo das Sociedades* or CGS) by the Portuguese Institute of Corporate Governance. This code's principles and recommendations pertain to the body of "soft law" and, thus, are not legally binding and cannot be enforced before a court.

In 2001, CMVM Regulation No 7/2001 adopted the "comply or explain" principle, whereby companies are required to disclose whether, and to what extent, they comply with the recommendations or to explain why they do not and proposed that companies issuing shares admitted to trading on a regulated market must annually disclose information on various aspects related

to corporate governance. This regulation also requires companies issuing shares to prepare a corporate governance report, either as an annex to the annual management report or in a separate chapter.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with publicly traded shares are subject to both mandatory and voluntary corporate governance requirements.

Mandatory Requirements

- disclosing annual reports and accounts;
- disclosing to the CMVM in the management annual report or in an attachment thereto a detailed report on the corporate governance with the following information:
 - (a) capital structure;
 - (b) any restrictions on the transferability of shares;
 - (c) qualified holdings in the company's share capital;
 - (d) identification of shareholders holding special rights and a description of those rights;
 - (e) control mechanisms within any employee participation schemes, where voting rights are not exercised directly by employees;
 - (f) any restrictions on voting rights;
 - (g) shareholder agreements that may lead to restrictions on the transfer of securities or voting rights;
 - (h) rules on the appointment and replacement of members of the management body and amendments to the company's by-laws;
 - (i) powers of the management body, particularly concerning resolutions on capital increases;
 - (j) significant agreements and amendments thereto;
 - (k) agreements between the company and the members of the management body or employees that provide for compensation in the event of resignation, dismissal without just cause, or termination of the employment relationship following a public takeover bid;
 - (l) key elements of the internal control and risk management systems implemented in the company regarding the process of disclosing financial information;
 - (m) statement on adherence to the corporate governance code to which the issuer is subject by a legal or regulatory provision;
 - (n) statement on compliance with any corporate governance code adopted voluntarily by the company;
 - (o) the location where the public can access the full text of the relevant corporate governance codes;
 - (p) composition and description of the functioning of the issuer's corporate bodies, as well as any committees that are created within them; and
 - (q) a description of the diversity policy applied by the company concerning its management and supervisory bodies, particularly in terms of age, gender, qualifications, and professional background, the objectives of this diversity policy, how it was applied, and the results in the reference period.
- the annual presentation, by the board of directors to the general meeting of shareholders, of a report explaining all the matters listed in the previous bullet point;
- disclosing to the public the following information:
 - (a) notice of shareholder meetings of companies issuing securities admitted to trading,

- inclusion of matters on the agenda and submission of resolution proposals;
- (b) modification, allocation, payment or exercise of any rights attached to securities admitted to trading or the shares to which they give rights, including the applicable procedures and the financial institution through which shareholders can exercise their property rights;
- (c) modification of bondholder rights resulting, inter alia, from changes to the loan conditions or interest rate;
- (d) share issuances, including associated privileges, and information on any allocation, subscription, cancellation, conversion, exchange, or redemption procedures;
- (e) modification of the elements required for the admission of securities to trading;
- (f) acquisition and disposal of own shares, when, as a result, the percentage exceeds or falls below the limits of 5% and 10% of the voting rights;
- (g) resolution of the general meeting concerning the financial statements; and.
- (h) the total number of voting rights and share capital at the end of each calendar month in which an increase or decrease of that total number occurs.
- publishing on the company's website the remuneration policy of members of management and supervisory corporate bodies, including the voting results and the date of approval at the general meeting;
- preparing a clear and understandable report by the management body that provides a comprehensive overview of remuneration, including all benefits, regardless of their form, granted or due during the last financial year to each member of the management and supervisory bodies;
- having an internal procedure approved by the management body, with a prior binding opinion from the supervisory body, through which it periodically verifies whether the transactions that the company conducts with related parties are carried out within the scope of their regular activities and under market conditions;
- publicly disclose transactions with related parties the value of which is equal to or greater than 2.5% of their consolidated assets, or of their individual assets if they do not prepare consolidated accounts; and
- publicly disclose all the information received regarding qualified participations.

Voluntary Requirements

The CGS sets out several principles and best practices that should be adopted by these companies, particularly concerning ESG, which is deemed a key goal of such corporate governance provisions.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

Until recently, companies have been following internationally recognised standards for the preparation of their sustainability reports, including the GRI Standards (Global Reporting Initiative), which are the most used, or the frameworks of the ISSB (International Sustainability Standards Board), the TCFD (Task Force on Climate-Related Financial Disclosures), or the TNFD (Taskforce on Nature-Related Financial Disclosures).

However, the latest EU directive on corporate sustainability reporting (CSRD, Directive 2022/2464) demands the use of European reporting standards, the ESRS (European Sus-

tainability Reporting Standards) and the application of the European Taxonomy.

In today's world, there is little doubt that companies must commit to respecting human rights and minimising their impact on the environment. Sustainability reporting is no longer limited to traditional financial metrics – it must also reflect both quantitative and qualitative information concerning a company's environmental, social, ethical, and human rights practices, as well as its stance on issues such as corruption. Younger generations, including Millennials and Generation X, place increasing importance on responsible investment and believe that it is possible to achieve competitive returns by incorporating ESG factors into investment decisions.

The new European regulatory duties have a systemic and cross-cutting effect. They focus on information provision but also require strategic definition and rigorous commitment. Decisions based on immediate profits compromise long-term sustainability as well as the longevity of the organisation. To mitigate this risk, companies should adopt governance models that encourage sustainable investments, linking bonuses to behaviours related to good ESG practices. Companies must find a way to leverage substantive sustainable business practices for competitive differentiation. This approach will result in a broader vision where financial gains go hand in hand with positive social and environmental impact. The companies that successfully balance purpose and profits through sustainability leadership will be best positioned for long-term success.

2.2 ESG Considerations

According to the CSC, the management report prepared by the management body should include not only financial matters but also rel-

evant information on environmental issues and employees' issues.

Furthermore, large companies of public interest must also include in their management report a non-financial statement with information that enables stakeholders to understand the impact of the company's activities in relation to environmental, social and employee issues, gender equality, non-discrimination, respect for human rights, corruption and bribery. The information must include the policies of the company regarding these issues and the results thereof as well as the associated risks.

The CSG also encourages the existence of mechanisms within companies for collecting and processing data on social and environmental sustainability. These mechanisms are intended to assist the management body in identifying risks and formulating appropriate strategies to mitigate them. Additionally, companies are expected to disclose how they address climate change and its related challenges.

The CSRD imposes several sustainability reporting obligations applicable not only to large companies but also to small and medium-sized companies deemed of public interest. Only micro-companies are excluded. For this purpose, EU law deems of public interest the following companies:

- with publicly traded shares;
- credit institutions;
- insurance companies; and
- designated by member states as public-interest entities.

Reporting obligations will include:

- evaluating the business model's resilience to sustainability risks, opportunities related to sustainability and plans for aligning with sustainable economy transitions and the Paris Agreement goals;
- establishing time-bound sustainability targets, including greenhouse gas reduction goals, and reporting progress and scientific validity of targets;
- describing the role and expertise of management bodies in sustainability matters;
- providing an overview of sustainability policies and incentive schemes linked to sustainability for management bodies;
- implementing due diligence processes, identifying and managing adverse impacts, and actions taken to mitigate these impacts;
- setting out the principal sustainability-related risks and dependencies, and how these are managed; and
- disclosing relevant indicators related to the points above.

Penalties shall be applicable to infringements of reporting obligations.

Portugal has introduced a transitional period for the full application of the CSRD, resulting in a staggered implementation calendar:

- For large public interest companies, the CSRD is applicable in the current year for the 2024 financial year.
- For all other large companies, the CSRD is applicable in 2028 for the 2027 financial year.
- For small and medium-sized public interest companies, the CSRD is applicable in 2029 for the 2028 financial year.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management Principal Bodies

The bodies involved in the governance and management of a company are:

- the sole director or board of directors in S.A. companies (in the event the share capital exceeds EUR250,000, administration must be carried out by a board of directors);
- managers in Lda companies; and
- the supervisory board, sole auditor, audit committee or general and supervisory board (depending on the corporate model adopted).

The board of directors and the sole director in S.A. companies or managers in Lda companies have exclusive and full powers of representation of the company. They are executive corporate bodies, in charge of managing the company. The company is bound by their acts executed or ratified by the majority of the directors, unless the articles of association provide otherwise, in which case a smaller number of directors may be sufficient.

The supervisory board, sole auditor or general board are responsible for the supervision of the company, particularly in relation to financial and accounting matters. The sole auditor and some of the members of the boards must be a statutory auditor (*Revisor Oficial de Contas* or ROC).

Lda companies that do not have a board of auditors must appoint an official auditor to carry out the supervision of the accounts if, for two consecutive years, the company exceeds at least two of the following thresholds:

- a total balance sheet value of EUR1,500,000;

- total net sales and other income of EUR3,000,000; and/or
- an average number of 50 employees.

3.2 Decisions Made by Particular Bodies Directors/Manager

Decisions taken by these bodies typically concern:

- the day-to-day management of the company;
- preparation of annual reports and accounts to be submitted for shareholders' approval;
- opening or closing of company branches or establishments;
- changes in the company's organisational structure; and
- hiring and termination of employment contracts.

In S.A. companies, directors have the authority to dispose of and encumber real estate assets.

Supervisory Bodies

Supervisory bodies have no management powers and are responsible, in particular, for:

- supervising the management of the company, and ensuring compliance with the law and the articles of association;
- ensuring the proper maintenance of the company's books and accounting record;
- checking the cash holdings and inventory of assets or securities of the company;
- verifying the accuracy of the financial statements;
- preparing an annual report on its activities and issuing an opinion on the management report and on the financial statements; and
- receiving reports of irregularities submitted by shareholders, company employees, or others.

3.3 Decision-Making Processes Directors/Manager

In the event these bodies are composed of several members, a specific process must be followed for the resolution to be valid, which normally takes place at a meeting convened for such purpose.

The board of directors shall meet monthly if not set out otherwise in the by-laws.

Resolutions are taken by the majority of the directors. Each director has one vote, and directors may not vote on matters in which they have a conflict of interest with the company. The chairman of the board of directors has a casting vote if granted by the articles of association or if the board is composed of an even number of directors.

Minutes must be drawn up for each meeting of the board of directors, recording the matters discussed and approved at the meeting, and must be signed by all directors present at the meeting.

Supervisory Bodies

In the event these bodies are composed of several members they shall meet at least once every quarter, and their resolutions shall be adopted by majority vote.

The chairman of the supervisory board has a casting vote if granted by the articles of association or if the board is composed of an even number of directors.

The minutes of each meeting shall be drawn up, and must be signed by all members present.

4. Directors and Officers

4.1 Board Structure

Board of Directors' Structure in S.A. Companies

The structure of the board of directors in an S.A. company is directly related to the structure of the respective supervisory board. There are three main mandatory governance models, which may slightly differ:

- The traditional or classic model includes a board of directors and:
 - (a) a sole auditor;
 - (b) supervisory board; or
 - (a) supervisory board and a statutory auditor (ROC) or an official auditing company (SROC).
- The Anglo-Saxon model includes a board of directors, including an audit committee and a statutory auditor.
- The German model includes an executive board of directors, general and supervisory board and statutory auditor.

Board of directors

Legal persons may be appointed as directors of a company but they must appoint an individual to act as director in his/her own name.

The board of directors is composed of any number of members, but with a minimum of two.

Supervisory board

The supervisory board comprises a minimum of three effective members. One of its permanent members and one of the substitutes must be a statutory auditor and cannot be a shareholder of the company. In companies with publicly traded shares, the supervisory board must be composed of a majority of independent members.

The most complex supervision structure that includes the supervisory board and the statutory auditor (who cannot be a member of the corporate bodies of the company) is mandatory for:

- companies with publicly traded shares; and
- companies that exceed two of the following limits:
 - (a) a total balance sheet value of EUR20,000,000;
 - (b) net turnover of EUR40,000,000; and/or
 - (c) an average of 250 employees.

Sole auditor

A sole auditor may be appointed instead of the supervisory board. It supervises the direction of the company. It must be a statutory auditor or an official auditing company. It cannot be a shareholder of the company. The company will always have a substitute auditor that shall also be an official auditor. Except for companies following the Anglo-Saxon model, the governance structure of a sole director may only be adopted if the company's share capital does not exceed EUR200,000.

Audit committee

This committee comprises a minimum of three effective members, some of which are non-executive members of the board of directors. In companies with publicly traded shares, most of these members must be independent. In listed companies and companies exceeding two of the limits set out under *Supervisory board* above, at least one of the members must be independent and have an appropriate degree and expertise in auditing and accountancy.

Executive board of directors

This board comprises any number of directors as set out in the articles of association. The company may only have a sole director if the share

capital is below EUR200,000. It carries out the company's executive functions.

General board

It comprises the number of members set out in the articles of association but not less than the directors.

They cannot be directors of the company.

Secretary of the company

Regardless of the governance model adopted, listed companies must appoint a company secretary as well as a substitute.

Lda Board Structure

The company is managed by one or more managers (*gerentes*), who must be individuals. These managers may or may not be shareholders.

4.2 Roles of Board Members

Provided authorised by the articles of association, the board may delegate, subject to certain limitations, the day-to-day management to one or more directors or to an executive committee.

The chairman of the board of directors is granted a casting vote in the board's resolutions in the following situations:

- when the board is composed of an even number of directors; and
- in other cases, if the articles of association provide for it.

The chairman of the executive committee is also granted a casting vote and he/she must:

- ensure that all information regarding the activity and decisions of the executive committee is provided to the other members of the board of directors; and

- ensure compliance with the delegation limits, the company's strategy, and the duties of collaboration towards the chairman of the board of directors.

4.3 Board Composition Requirements/Recommendations

In listed companies and public interest entities, the proportion of individuals of each gender newly appointed to each management and supervisory body of each company cannot be less than 33.3%.

To ensure the desirable agility of the executive management's functioning and a balanced and appropriate diversity of skills, knowledge, and professional experience, the CGS sets out the following principles regarding the composition of the board of directors:

- The number of executive directors should take into account the size of the company, the complexity and geographical dispersion of its activity, and the costs.
- The number and qualifications of non-executive directors should be adequate to provide the company with a balanced and appropriate diversity of skills, knowledge, and professional experience.

4.4 Appointment and Removal of Directors/Officers

Appointment of Directors

As a general rule, the directors are appointed in the incorporation deed or by the shareholders' meeting. Directors must formally accept their appointment and declare that they are not aware of any circumstances that may prevent them from being appointed.

In the event the company adopts the German model, and provided the by-laws do not set out

otherwise, the general and supervisory board is in charge of appointing the members of the executive board of directors.

The directors are appointed for a period set out in the company's by-laws, which cannot exceed four years. However, directors may be re-elected and remain in office after the original term has elapsed until new appointments are made.

Listed companies must include in the by-laws a provision enabling minority shareholders, representing at least 10% of the share capital, who have voted against the approved proposal for the appointment of directors, to appoint at least one director.

The board may also elect a new member in the event one director is permanently absent and the board is unable to operate. Otherwise, the supervisory board of the audit committee will appoint him/her. Such election must be ratified by the shareholders' meeting.

Removal of Directors

Any member of the board of directors can be removed by resolution of the general meeting at any time.

A director appointed according to special rules (such as those that must be adopted by listed companies) cannot be removed without a just cause if shareholders representing at least 20% of the share capital have voted against the resolution for their removal.

A director may resign from their position by sending a letter to the chairman of the board of directors or, if the chairman is the one resigning, to the supervisory board or the audit committee.

In the event that, after the appointment of any director, any incompatibility or incapacity occurs that would prevent such director from being appointed, the supervisory board or the audit committee shall declare the termination of his/her office if the director fails to resolve the issue, or does not resign.

Restrictions on Appointment

Persons who do not have full legal capacity cannot be directors.

Persons disqualified from engaging in commerce, as well as from holding any position as an officer of a commercial or civil company, as a consequence of an insolvency due to misconduct or negligence, cannot be directors.

Directors may not perform any temporary or permanent work in the company, or in companies that are in a controlling or group relationship therewith, under any employment contract, whether subordinate or autonomous. They also cannot enter into any such contracts for the provision of services when their role as a director ends.

Directors may not engage in any activity competing with the company, either on their own or on behalf of others, nor may they hold positions in a competing company or be appointed on behalf of or in representation of such a company.

Members of the executive board of directors in the German model are not required to be shareholders but they cannot be:

- members of the general and supervisory board;
- members of the supervisory bodies of companies that are in a controlling or group relationship with the company in question; or

- spouses, relatives, and kin in the direct line, and up to the 2nd degree, inclusive, in the collateral line, of the persons mentioned in the previous bullet point.

Additionally, a company can set eligibility criteria for the role of director, such as requiring professional experience or specific qualifications.

4.5 Rules/Requirements Concerning Independence of Directors

Restrictions on appointments referred to in 4.4 **Appointment and Removal of Directors/Officers** also serve as independence requirements.

The CSC also sets out that directors of the company or of a company in a domain or group relation with the company cannot be appointed as members of the supervisory board, sole auditors or statutory auditors.

The CGS sets out recommendations regarding the independence of directors and specifically defines an independent person as not associated with any specific interest group within the company, nor in any situation likely to affect their impartiality in analysis or decision-making.

4.6 Legal Duties of Directors/Officers

Directors are required to comply with several legal duties, including:

- a duty not to exceed the corporate purpose or engage in acts contrary thereto;
- a duty of care, demonstrating availability, technical competence, and knowledge of the company's activities appropriate to their roles, while exercising the diligence of a prudent and organised manager in this context;
- a duty of loyalty in the interests of the company, considering the long-term interests of the shareholders and weighing the interests of other relevant parties for the company's sustainability, such as its employees, clients, and creditors;
- a duty of vigilance, particularly by immediately convening a shareholders' meeting upon acknowledging that the annual or intermediate accounts evidence a loss of more than half of the company's share capital;
- a duty of non-competition, whereby, during the period for which directors were appointed, they may not perform any temporary or permanent functions in the company, or in companies that are in a controlling or group relationship therewith, under any employment contract, whether subordinate or autonomous; they also cannot enter into any such contracts for the provision of services when their role as a director ends;
- a duty to inform the company of the number of shares and bonds of the company that they (or any person directly related to them) hold, as well as all their acquisitions, encumbrances, or cessations of ownership, for any reason, of shares and bonds of the same company and of companies with which it is in a controlling or group relationship.
- a duty to prevent any conflict of interest with the company by informing the other directors thereof and not taking part in the relevant decisions that could be affected by such conflict;
- a duty to prepare and submit to the competent corporate bodies the management report, including the non-financial statements or a separate report with the same information, where applicable, the annual accounts, as well as other financial statements required by law for each financial year;
- a duty to take the necessary measures to resolve discrepancies between acts, their registration, and the publications; and

- a duty to request the convening of the annual general meeting and present the necessary proposals and documentation for the resolutions to be made by the shareholders.

4.7 Responsibility/Accountability of Directors

Liability

- Directors are liable to the company for damages caused thereto by acts or omissions carried out in breach of legal or contractual duties, unless they prove that they acted without fault.
- Directors are also liable to shareholders, company creditors and third parties for any individual damage their acts may cause them.
- Director's liability is joint and several.
- Directors bear subsidiary liability towards third parties and jointly between them for all the taxes concerning the company's financial year, unless they are able to prove that the insufficiency of the company's assets to cover tax liabilities was not due to any fault on their part.
- The consent or favourable opinion of the supervisory board does not exempt the directors from liability.

Exclusion

- Liability is excluded if directors can prove that they act in an informed manner, free from any personal interest, and according to business rationality criteria.
- Directors who were not part of a resolution or who voted against it are not responsible for the damage resulting therefrom. In such cases, directors may record their vote against it within five days, either in the respective minutes book, or addressing it, in writing, to the supervisory body or before a notary or a registrar. Nevertheless, a director who did not exercise the right of opposition granted by

law, when in a position to do so, is jointly liable for the acts he/she could have opposed.

- The liability of directors towards the company does not apply when the act or omission is based on a resolution by the shareholders, even if it is not valid.

Guarantee

The liability of a director must be guaranteed by means of a bond or an insurance policy with a minimum coverage of EUR250,000 for listed companies and EUR50,000 for other types of companies.

Non-executive and non-remunerated directors are exempt from providing a bond.

The bond may be waived by the company's by-laws or by means of a resolution of the shareholders' meeting.

Joint Liability With Directors

The legal person appointed as director is jointly liable with the individual he/she appoints to act as director in his/her own name.

Shareholders with a special right to appoint a director are jointly liable with him/her before the company and the other shareholders in the event of fault in such election.

4.8 Consequences and Enforcement of Breach of Directors' Duties

The Company

By means of a resolution of the shareholders' meeting duly convened for such purpose, the company may dismiss the directors due to a breach of their duties which is deemed a just cause for the dismissal.

The company may file a liability claim against the directors based on a prior resolution of the

shareholders, passed by a simple majority, and must be initiated within six months of the resolution.

The Shareholders

Regardless of any claim for compensation for individual damage they may have incurred, one or more shareholders holding at least 5% of the share capital, or 2% in the case of a company with publicly traded shares, can file a lawsuit against directors seeking compensation for damages the company has incurred, in favour of the company, when the company itself has not pursued such a claim.

Shareholders holding at least 10% of the share capital may file for the judicial removal of a director if the shareholders' meeting has not yet been convened for that purpose. Any shareholder, regardless of the percentage of the share capital participation, may file for the judicial removal of a director in the event of insider trading.

Company Creditors

If neither the company nor its shareholders file a lawsuit against the directors whose wrongful conduct has led to the company's inability to meet its financial obligations, the company's creditors are entitled to file such a claim.

Third Parties

Any third party that may have incurred damages due to a director's breach of duties may also file a claim against them.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other Bases for Claims – Criminal Liability

Directors may also be held criminally liable for intentionally:

- failing to convene a shareholders' meeting upon becoming aware that the annual or intermediate accounts evidence a loss of more than half of the company's share capital, and failing to propose the dissolution of the company or the reduction of its share capital;
- omitting acts required for the realisation of the share capital;
- acquiring for the company its own shares, or financing or guaranteeing such acquisition, in violation of the law;
- illicitly distributing the company's assets;
- not convening the meetings required by law or inserting therein false information;
- obstructing the proper functioning of the general meeting or assisting anyone to participate therein by presenting false documents;
- refusing, in any meeting, information which, by law, is mandatory and that has been requested in writing for the approval of the financial year accounts;
- providing false or incomplete information when obliged to provide accurate information regarding the company;
- refusing to draw up the minutes of the meetings;
- preventing the supervision of the company;
- failing to comply with the requirements for the issuance of the shares certificates; and
- refusing or delaying access to the documents required for the preparation of any shareholders' meeting.

Limitation of Liability

The liability of a director cannot be limited. The CSC provides that any provision that excludes or limits the liability of directors is null and void. The company may, however, resolve to waive its right to claim compensation from a director. This requires a resolution of the shareholders' meeting and must not be opposed by minority

shareholders representing at least 10% of the company's share capital.

A lawsuit filed by minority shareholders (as described in **4.8 Consequences and Enforcement of Breach of Directors' Duties**) against directors, seeking compensation for damages incurred by the company cannot be subject to any prior opinion or resolution of the shareholders or prior judicial decision thereon. Such provisions would be null and void.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Remuneration of directors is determined by the general meeting of shareholders or by a committee appointed thereby for such purpose. In companies adopting the German model, the remuneration of directors may also be determined by the general and supervisory board or by a committee it appoints.

Directors' remuneration shall comprise a fixed and a variable component such as profit sharing.

Companies issuing publicly traded shares are required to approve a remuneration policy that shall be submitted by the remuneration committee (or by the board of directors in the event the committee has not been appointed) to the shareholders' approval every four years and whenever there is a relevant change of the remuneration policy. However, in exceptional cases, these companies may derogate such policy in the event it is deemed necessary to serve their long-term interests and sustainability or to ensure their viability.

The remuneration policy for directors of listed companies must be clear, transparent, and consistent, aiming to align the interests of the

directors with those of the company and its shareholders. The remuneration should reflect the value of the directors' work and encourage their efforts in managing the company, with a view to ensuring the company's sustainability in the markets.

The company is forbidden from granting loans or credit to directors, making payments on their behalf or providing guarantees in respect of their obligations. Additionally, advance payments of remuneration may not exceed one month's salary.

The CGS reflects the idea that the remuneration of directors should ensure alignment with the long-term interests of the shareholders and promote the sustainable operation of the company. It recommends the establishment of a remuneration committee and advocates that part of the remuneration for directors (excluding non-executive directors) should be variable. This variable component should reflect the company's sustained development without encouraging excessive risk-taking. Moreover, it recommends that a portion of the variable remuneration be deferred.

4.11 Disclosure of Payments to Directors/Officers

Please refer to **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**, **5 Shareholders** and **6 Corporate Reporting and Other Disclosures**.

The remuneration policy of companies with publicly traded shares must be published immediately on the company's website following its approval by the shareholders' general meeting. This publication must clearly indicate the voting results and the date of approval. The policy must remain freely accessible to the public for as long as it remains in effect.

Furthermore, the board of directors is required to issue annually a clear and comprehensive report (or chapter in the annual management report to be submitted with the annual accounts) providing a comprehensive view of remuneration, including all benefits allocated or due in the previous financial year to each member of the administrative and supervisory bodies according to the remuneration policy, including newly appointed members and former members. This report is submitted to the annual general meeting of shareholders for approval of the accounts, after which it is also published on the company's website where it shall remain available for ten years.

The CGS recommends that the disclosure of the amounts paid to any member of the company's body or committee due to the termination of their duties must be made either in the governance report or in the remuneration report.

Shareholders with shares representing at least 1% of the share capital may require information and documents on the amounts paid in the last three years to corporate body members.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Relationship Between the Company and its Shareholders

A company is a legal person distinct from its shareholders. Although shareholders may serve as directors, maintaining a clear separation between ownership and management allows the company to appoint qualified professionals to handle its day-to-day operations. However, external managers sometimes take advantage of their positions, making self-serving decisions

or even misusing company funds. Shareholders are not only entitled to appoint and dismiss management members but also to control how the company is managed and pursue claims against directors who cause harm to the company through mismanagement (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**). Shareholders also have a duty of loyalty and co-operation with the company, meaning that they should not act against the company's interests.

The CGS chapter regarding relations between the company and its shareholders sets out the guiding principle that the company's management should consider the interests of shareholders when making decisions.

Rules and Requirements of the Relationship

The relationship between the company and its shareholders is complex and defined by a set of rules and agreements that regulate the rights and duties of the shareholders, as well as their liability towards the company and third parties.

The shareholders' liability is limited to the value of the share they have subscribed in the company's share capital, meaning that the creditors of the company cannot pursue the personal assets of the shareholders.

The main obligations of a shareholder set out in the CSC are paying the initial contribution and participating in the losses of the company.

Core rights

The core rights of shareholders are:

- to participate in the distribution of profits;
- to participate in company resolutions, which includes the right to vote at the general meeting;

- to receive information regarding the company; and
- to be appointed as a member of the corporate bodies of the company

Special rights

The special rights of shareholders are granted by the by-laws to one or more shareholders, giving them an advantage over the others. For instance, in Lda companies, shareholders may be granted the right to a percentage of profits greater than their stake in the share capital, or the right to be the company's director. In S.A. companies, the special rights are allocated to categories or classes of shares.

Other rights

Other rights of the shareholders are the preferential right to subscribe to capital increases, and protection against arbitrary exclusion by the majority shareholders.

In Lda companies, either the shareholder is entitled to relief himself/herself from the company or the company may, under certain requirements, resolve on the exclusion of the shareholder.

Available Record of the Shareholders of a Company

The rules for publicising a company's shareholders depend on the type of company.

Lda companies

Information on shareholders is compulsorily registered with the Commercial Registry Office and afterwards published on the Official Website for Corporate Acts and Other Entities. It is publicly available upon request.

S.A. companies

Information on the shareholders of an S.A. company is contained in the company's shares ledger, which is not publicly available.

5.2 Role of Shareholders in Company Management

The extent of shareholder involvement in company management depends on the type of company.

In Lda companies:

- The CSC requires prior shareholder approval for key acts, including:
 - (a) calling or reimbursing supplementary contributions;
 - (b) redeeming, acquiring, encumbering, or dividing own shares;
 - (c) the exclusion of shareholders;
 - (d) the removal of managers and members of the supervisory body;
 - (e) the approval of the management report and annual accounts, the allocation of profits, and the treatment of losses;
 - (f) the discharge of liability of managers or members of the supervisory body;
 - (g) the filing of legal actions by the company against managers, shareholders, or members of the supervisory body, as well as the withdrawal and settlement thereof;
 - (h) amendments to the articles of association; and
 - (i) the merger, demerger, transformation, and dissolution of the company, and the resumption of activity by a dissolved company.
- Even when shareholders are not part of the company's management, they are often well informed about the company's affairs. Moreover, shareholders may remove managers at any time, with or without just cause.

In S.A. companies:

- In contrast, in this type of company shareholders typically do not have the same degree of influence over the company's management, which is vested in a management body that differs according to the governance model adopted (as mentioned in **4.1 Board Structure**).
 - Unlike in Lda companies, shareholders of an S.A. are required to resolve on management matters only if the board of directors submits such matters for their approval. This may apply, for example, to decisions regarding:
 - (a) the acquisition, disposal, or encumbrance of real estate;
 - (b) the provision of guarantees or security (personal or in rem) by the company;
 - (c) the opening or closure of establishments or substantial parts thereof;
 - (d) significant expansions or reductions of the company's business activities;
 - (e) major changes to the company's internal organisation; and
 - (f) the initiation or termination of long-term and significant co-operation with other companies.
 - There are, however, matters that are specifically reserved to shareholders of an S.A. by law or by the articles of association, such as:
 - (a) approval of accounts (annual meeting mentioned in **5.3 Shareholder Meetings**);
 - (b) amendments to the articles of association; and
 - (c) company demerger or dissolution.
- (a) approve the annual management report and accounts;
 - (b) decide on profit allocation;
 - (c) assess the management and supervision, dismiss officers or express lack of confidence; and
 - (d) elect members of corporate bodies.
- Other situations when a shareholders meeting may be required:
 - (a) by the management body (see **4.6 Legal Duties of Directors/Officers**) upon acknowledge that the annual or intermediate accounts evidence a loss of more than half of the company's share capital;
 - (a) by shareholders representing at least 5% of the share capital or at least 2% of the share capital in companies with publicly traded shares;
 - (a) by the supervisory body in the event the chairman of the meeting does not convene it;
 - (b) by the ROC upon acknowledging severe difficulties of the company; and
 - (c) by the court upon request of any shareholder if the shareholders do not approve the annual accounts.

5.3 Shareholder Meetings

Required Shareholders Meetings

- For both S.A. and Lda companies, a general meeting must be held annually, within three months after financial year end, to:

Rules Governing the Holding and Conduct of a Shareholders' Meeting

The convening of general meetings varies depending on the type of company.

For Lda companies

- The convening authority is the manager(s). The chairman is the shareholder present who holds or represents the largest capital share, or, if tied, the oldest.
- Notice is made by registered letter sent at least 15 days in advance, unless otherwise required by law or by-laws;
- Minutes must be signed by all shareholders who attend.

- Each cent of nominal share value equals one vote. The articles may grant up to two votes per cent as a special right, provided it applies to quotas totalling no more than 20% of the share capital. Unless otherwise stated by law or the articles, resolutions pass by a majority of votes cast, excluding abstentions.
- A shareholder may be represented by a signed written document addressed to the chair of the meeting. Voluntary representation is only allowed to the shareholder's spouse, ascendants, descendants, or another shareholder, unless the articles of association expressly allow other representatives.

For S.A. companies

- The convening authority is the chairman of the general meeting board. The articles may provide for the chairman's election; failing that, the chair is the president of the audit board, audit committee or supervisory board.
- A notice must be published. The articles may require additional media (eg, newspapers). Holders of registered shares receive a registered letter or, with consent, an email with read receipt.
- At least one month must elapse between publication of the notice and the meeting; letters/emails must be sent at least 21 days in advance of the meeting.
- Minutes must be signed by the chairperson and the secretary.
- Unless otherwise stated in the articles of association, each share carries one vote. In general, resolutions are approved by a majority of votes cast, regardless of the share capital represented, unless the law or articles state otherwise. Abstentions are not counted.
- A shareholder may be represented by a signed written document addressed to the chair of the meeting.

Quorum for shareholders' meetings

- On first call, any number of shareholders present or represented may deliberate, except when by-laws provide otherwise or when the meeting is to decide on:
 - (a) an amendment to the by-laws;
 - (b) a merger, demerger, transformation, or dissolution of the company; and
 - (c) other matters for which the law requires a qualified majority without specifying its extent.
- On second call, there is no minimum quorum requirement.

The venue of the meetings

- Meetings are held at the registered office or, if space is inadequate, elsewhere in Portugal chosen by the chairperson.
- Unless the articles provide otherwise, meetings may be held by electronic means.

Shareholders may also pass unanimous written resolutions or hold a universal meeting without prior formalities when all are present and agree to meet and resolve.

5.4 Shareholder Claims

Shareholders may bring claims against the company or its directors as mentioned in **4.8 Consequences and Enforcement of Breach of Directors' Duties**.

5.5 Disclosure by Shareholders in Publicly Traded Companies

According to the CVM, shareholders in publicly traded companies must notify the issuer and the CMVM in the event their holding exceeds or falls below the thresholds of 5%, 10%, 15%, 20%, 25%, one-third, 50%, two-thirds and 90% of the voting rights corresponding to the share capital of an issuer admitted to trading on a regulated

market, no later than four trading days after the change or the date on which it became known.

Also, holders of a qualified participation in publicly traded companies must inform the CMVM, upon its request, of the origin of the funds used for reaching or exceeding this threshold.

Furthermore, EU anti-money laundering directives created the RCBE according to which companies must disclose their ultimate beneficial owner (UBO). However, companies whose shares are already traded on a regulated market and subject to EU-level (or equivalent) transparency requirements on ownership and voting rights may be exempt from RCBE registration.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Annually, the directors are required to prepare and submit to the shareholders the following:

- management report and the accounts;
- attachment to the accounts; and
- non-financial statements.

The shareholders must pass a resolution on these documents.

In a parent company subject to consolidated accounts, the directors shall also prepare on an annual basis all the respective consolidated documents.

In companies with publicly traded shares, directors must also prepare a detailed report on the corporate governance management and disclose it to the CMVM.

Companies with publicly traded shares are required to file biannually an interim management report and condensed financial statements.

6.2 Disclosure of Corporate Governance Arrangements

Please refer to **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** regarding disclosure of corporate arrangements and to **2.2 ESG Considerations** regarding the CSRD on reporting obligations.

6.3 Companies Registry Filings Registration of Companies

The incorporation of a company in Portugal must be made by means of a deed, and registered with the Commercial Registry Office within two months.

For the registration of the company, the following documents must be filed:

- deed of incorporation, including the by-laws;
- declarations of the members of the corporate bodies accepting their appointment; and
- information on the UBO.

Failing to file any of these documents will prevent the registration of the company. Upon verifying that any of the required documents is missing or incorrectly drafted, the Registry Office will request the company to submit the correct document within five business days, failing which the registration application will be refused.

After the registration, the incorporation of the company is published on the Official Website for Corporate Acts and Other Entities. This platform publishes key information about companies, including, for example, the composition of corporate bodies and changes to the by-laws.

Afterwards, the respective UBO declaration must be filed with the RCBE within 30 days of the company's incorporation.

Publicly Available Information

Acts and facts registered in the commercial registry office are publicly available, including the documents filed therewith. The aim of the Commercial Registry Office is to publicise the legal situation of companies and other commercial entities.

Powers of the Registry Office

Registration requests are assessed under the principle of legality – ie, the feasibility of the registration application to be made by transcription must be assessed according to the applicable legal provisions, the documents presented, and previous registrations, particularly verifying the legitimacy of the interested parties, the formal regularity of the titles, and the validity of the acts contained therein. In essence, only facts that are legally subject to registration, and that are properly substantiated through adequate documentary evidence, may be recorded in the official registry. The registrar's role is to qualify the act by confirming the legal validity of the request and the adequacy of the supporting documents. Once the registrar is satisfied that the legal requirements have been met, the act is entered into the registration system.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The appointment of an external auditor is required in the cases mentioned in **4.1 Board Structure**.

External auditors:

- serve as one of the primary protectors of corporate governance in any entity;
- report the state of a company's financial situation and certify the validity of financial reports that may have been released. All the information must be accurate and reliable;
- introduce policies to ensure accountability in the company;
- help promote corporate governance by conducting periodic risk assessment;
- review the security measures that a firm has in place against corporate fraud or corruption; and
- analyse the overall risk tolerance of the firm and all the initiatives of the company for mitigating risks.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Directors are required to prepare several documents assessing management risk and internal controls, such as the management report, the attachment to the accounts, the non-financial statements, the annual report on corporate governance and the interim management report. Such documents are afterwards either explained or submitted for the shareholders' approval.

Please refer to **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** and **3 Management of the Company**.

PUERTO RICO



Law and Practice

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Ferraiuoli LLC

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Ferraiuoli LLC is one of Puerto Rico's leading full-service corporate law firms. The firm provides comprehensive legal advice and representation to industry-leading private and publicly owned companies, as well as to financial institutions, on corporate, tax, labour, litigation and regulatory issues, among other matters. Skilled in structuring complex corporate structures, Ferraiuoli LLC's corporate attorneys handle entity selection and formation, registration

to do business, governance and fiduciary duty inquiries, contract review and negotiation, and work on all types of transactions across multiple industries. They also have extensive experience in due diligence initiatives and local and cross-border mergers, asset sales and business unit divestitures, stock sales and capitalisations, and restructurings. The firm provides services to clients from Puerto Rico, the US mainland, Europe, the Caribbean, and Latin America.

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Ferraiuoli

1. Introductory

1.1 Forms of Corporate/Business Organisations

The principal forms of corporate/business organisations in Puerto Rico are “*corporations*” and “*limited liability companies*” (LLCs) – the latter having gained popularity among business owners given the particular advantages they offer, including:

- the freedom to structure management (ie, member-managed, manager-managed, or with a centralised management structure such as board-managed);
- not being required to file and disclose financial statements with the Puerto Rico Department of State;
- enjoying streamlined corporate formalities; and
- having the option to be taxed as a pass-through entity or as a regular corporation.

Please note that although there are publicly traded companies organised under the laws of Puerto Rico that trade in national stock markets (ie, NYSE and AMEX) and over-the-counter markets (ie, NASDAQ), this chapter will not cover corporate governance requirements applicable to publicly traded companies under United States federal securities laws and regulations and applicable securities exchanges rules and regulations.

1.2 Sources of Corporate Governance Requirements

There are two main sources of corporate governance requirements.

- Legal sources: Puerto Rico Corporations and LLCs are subject to the requirements of the Puerto Rico General Corporations Act of

2009, as amended (the “*Corporations Act*”) and regulations published under it, as well as case law from the Puerto Rico Supreme Court. It is important to note that the Corporations Act is modelled after the Delaware General Corporation Law, and that the Puerto Rico Supreme Court has stated that judicial decisions from Delaware courts in connection with the interpretation of the Delaware General Corporation Law shall be highly persuasive and illustrative before Puerto Rican courts. This principle of interpretation has not been expressly extended by the Puerto Rico Supreme Court to Delaware court decisions interpreting the Delaware Limited Liability Company Act (the “*Delaware LLC Act*”) however, it seems highly probable that the same principle would apply.

- Organisational documents: A corporation’s or LLC’s organisational documents are an important source of corporate governance requirements, rights and obligations. A corporation’s articles of incorporation, by-laws and shareholders’ agreement may include particular provisions regarding voting requirements, transfer restrictions, meetings and shareholder rights, among others. Note that although a shareholders’ agreement is an important source of corporate governance for corporations, the Corporations Act does not impose on a corporation or its shareholders the obligation to adopt such a document.
- Although the Corporations Act has default provisions applicable to LLCs, an LLC’s limited liability company agreement is the principal source of corporate governance requirements, rights and obligations. This is because one of the LLC’s principal benefits is the freedom provided to the members in determining the governance structure of the company, the formalities (if any) that shall be

required, and ultimately how the company is managed.

- The Corporations Act does not impose on the members of an LLC the obligation to adopt a limited liability company agreement. However, unlike Delaware law, which includes oral, written or implied forms of a limited liability company agreement, the Corporations Act defines the limited liability company agreement as a written agreement. If no limited liability company agreement is adopted, the LLC will be subject to the default provisions contained in the Corporations Act. For the purpose of this publication, the authors will treat LLCs as if a limited liability company agreement had been adopted.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Puerto Rican publicly traded companies registered with the Securities and Exchange Commission are subject to regulations promulgated under the Securities Act of 1933 and the Securities Exchange Act of 1934, and to such other rules and corporate governance requirements imposed by the exchanges in which their securities are traded.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

A recent development in corporate governance is the amendment of the Corporations Act in December 2015 to allow for the organisation, merger and/or conversion of public benefit corporations (“*Benefit Corporations*”) in Puerto Rico. Benefit Corporations that are organised under the Corporations Act are required to file annual reports and social benefit reports, setting

forth the public benefit provided by the corporation.

One of the advantages of organising a Benefit Corporation is that its directors, in making their determinations, are allowed to consider factors other than the best interests of its shareholders (for example, they are allowed to take into consideration, among other things, the general public benefit pursued, the best interests of its employees and the community at large). In addition, directors of Benefit Corporations shall not be liable for any damages caused due to decisions made in good faith and in pursuit of the general public benefit set forth in the certificate of incorporation.

Additionally, in 2017, the Supreme Court of Puerto Rico decided that, in order to require that a corporation liquidate any assets still owned by it after the three-year period granted by the Corporations Act following dissolution has elapsed, the interested party must request that the court appoint one or more of the directors of the corporation to be trustees, or appoint one or more persons to be receivers, of and for the corporation, to take charge of the corporation’s property, as provided under Article 9.09 of the Corporations Act.

A major challenge in Puerto Rico is that the majority of private companies in the country are closely held family businesses that generally do not have the sophistication of larger businesses with regard to matters of corporate governance. Thus, given the nature of these companies, corporate governance formalities are not always strictly followed or enforced, and this may cause difficulties or problems when attempting to execute certain types of transactions, such as obtaining commercial financing or a merger and acquisition of an ongoing concern.

Another significant challenge for most closely held family businesses is the adoption and successful implementation of an orderly plan of succession that will smoothly transfer the management of the business from one generation to the next. Often, these companies are founded and managed by one individual who may not take the time to nurture or identify another person or persons to succeed them after their retirement or death. The lack of a generational transition plan has resulted in the termination of many successful businesses in Puerto Rico.

Due to their flexibility regarding governance, LLCs offer family and small businesses the ability to reduce recurring governance and other formalities.

As a result of the COVID-19 pandemic, and despite already being permitted under the Corporations Act, there has been an increase in questions and/or requests to update by-laws, limited liability company agreements and organisational documents to allow for remote meetings of shareholders, members, directors and managers.

2.2 ESG Considerations

In addition to existing regulations concerning the use of natural resources that extend from federal to local law (for example, regarding air and water pollution) which vary depending on the industry sector, Act 33-2019 adopted a new public policy to:

- address climate change;
- reduce and mitigate the effects of greenhouse gas emissions;
- address deforestation on the island;
- promote a sustainable economy; and
- incentivise renewable energy sources, as part of the government's energy diversifica-

tion and transformation policies under Act 82-2010 (Renewable Energy and Diversification) and Act 17-2019 (Energy Public Policy Act), among others.

Likewise, as previously mentioned in **2.1 Hot Topics in Corporate Governance**, in December 2015, the Puerto Rican government enacted Act 233-2015, which amended the Corporations Act to allow the creation of public benefit corporations. Public benefit corporations are required, among other things, to file annual reports and social benefit reports regarding:

- environmental matters (product cycle management, reduction of waste and residues, use of clean technologies, reduction of a negative environmental footprint, and responsible use of natural resources);
- corporate operations (information transparency, economic impact in the communities where the corporation operates, and health and safety initiatives); and
- human capital (policies and practices against discrimination, elimination of work violence, and development of human capital).

Also, the reports must set out the public benefits that the entity brings to the community in which it operates.

In addition, a significant number of companies practise various levels of corporate social responsibility. Generally, Puerto Rican companies and business leaders are actively involved in an array of non-profit entities that provide a wide variety of services and benefits to local communities.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

As a general rule, corporations are managed by or under the direction of a board of directors. This notwithstanding, the certificate of incorporation for certain types of corporations (eg, close corporations and non-profit corporations) could establish a different management structure, in which case the person or group of persons designated in the certificate of incorporation would assume all of the powers and responsibilities traditionally granted to the board of directors. Furthermore, the certificate of incorporation may grant to the board of directors the power to execute management agreements – provided, however, that the terms of such management agreement may not exceed three years. It is important to note that the board of directors of a corporation generally does not engage in or manage the daily operations of the corporation; instead, such responsibilities are delegated by the board of directors to the officers that it appoints.

Contrary to a corporation, an LLC is member-managed by default; however, the limited liability company agreement may provide for a centralised management structure similar to that of a corporation (ie, a board of managers and officers). As the name implies, in a member-managed LLC the members are responsible for the day-to-day operations of the company. In certain instances, the members may decide to appoint a manager, who does not have to be a member, to oversee the day-to-day operations of the company.

As mentioned in **1.2 Sources of Corporate Governance Requirements**, Delaware case law is highly persuasive in Puerto Rico. Although the Puerto Rico Supreme Court has yet to express

itself on the following matter, it is important to note that the Delaware Chancery Court has stated in *Obied v Hogan*, WL 3356851 (2016) that the choice of management structure chosen by the members shall have consequences when drawing case law as an analogy in order to solve a controversy. For example:

- if the members adopted a board of managers structure, corporate law may be applied by a court of law; or
- if the members adopted a member-managed structure, general partnership law may be applied by analogy in deciding the particular controversy.

3.2 Decisions Made by Particular Bodies

The board of directors of a Puerto Rican corporation is responsible for making key decisions and providing strategic direction to the corporation. Some of the major decisions made by the board of directors include the following:

- appointment of officers – the board appoints the Chief Executive Officer (CEO) and/or President, the secretary and any other officers of the corporation, and evaluates their performance regularly;
- financial oversight – the board reviews and approves the company's financial statements, budgets and major financial transactions;
- stock-related decisions – the board makes decisions related to dividends, stock issuances or repurchases;
- extraordinary transactions – the board evaluates and approves extraordinary transactions (such as potential mergers, acquisitions or divestitures, sale of substantially all or all of the corporate assets, or the dissolution or liquidation of the corporation) and recommends any such transaction to the shareholders of

- the corporation for their consideration and approval; and
- legal and regulatory compliance – the board ensures compliance with applicable laws, regulations and corporate governance.

The governance structure of a Puerto Rican LLC is generally set forth in the limited liability company agreement. The LLC can be member-managed, manager-managed or can even adopt a more traditional corporate board structure. Where the limited liability company agreement is silent, the holders of a majority of the company's membership interest shall control, but any member can bind the company before a third party.

3.3 Decision-Making Processes

The decision-making process for a board of directors and/or other governing bodies typically occurs through one of two methods:

- meetings; or
- written consent.

The Corporations Act does not impose a statutory requirement to hold a minimum number of board of directors' meetings, nor does it provide or establish specific guidelines as to how to conduct the order of business in a board meeting. The Corporations Act simply requires, unless otherwise stated in the certificate of incorporation or the by-laws, that the board of directors' meeting be held in person or by electronic means of communication (such as telephone or video conferences) provided that all members of the board of directors assisting such meeting can listen to each other simultaneously.

Furthermore, unless prohibited by the corporation's by-laws, any action required or permitted to be taken at any meeting of the board of directors may be taken without a meeting, if all mem-

bers of the board of directors consent thereto in writing, and such consents are filed with the minutes of the proceedings of the board of directors. Thus, any rules governing the meetings of the board of directors, such as minimum notification periods, frequency of meetings and quorum, are most commonly specified in the corporation's by-laws.

The Corporations Act does not govern the meetings of the members of an LLC, nor does it provide or establish rules governing the structure or process for the meetings of the members or any governing body. Given that the Corporations Act does not require that a meeting of the management body of an LLC be held, such requirements are generally established in the company's limited liability company agreement.

4. Directors and Officers

4.1 Board Structure

A typical board structure of a Puerto Rican corporation consists of one or more natural persons who are elected to act as directors of the corporation by the shareholders. In a standard board structure, all directors are elected for a one-year term, and shareholders vote for the entire board at the annual meeting.

However, a Puerto Rican corporation may choose to implement a staggered board structure, where the board is divided into multiple classes, with each class serving a different term length. For example, the board may be divided into three classes, where one class is elected for a one-year term, another for a two-year term, and the third for a three-year term. Each year, shareholders vote to elect directors for the class that is up for election, and this process is repeated over the years. The purpose of a staggered

board structure is to provide continuity and stability to the corporation's leadership.

In the case of an LLC, if the limited liability company agreement provides for a board structure, one salient difference is that a legal entity (as opposed to a natural person) may be a member of the board of an LLC.

4.2 Roles of Board Members

In a Puerto Rican corporation, there are no set roles for directors; nevertheless, if the corporation is so structured through its by-laws and/or certificate of incorporation, directors may hold various offices with particular roles, such as the following.

- The chairman of the board is usually responsible for leading board meetings and setting the agenda, and often acts as a liaison between the board and senior management.
- The vice-chairman is a senior board member who supports the chairman of the board, and may step in to fulfil their duties in their absence. The vice-chairman often plays a leadership role in board committees and provides guidance to other directors.
- The secretary of the board of directors of a Puerto Rican corporation must be present at all meetings of the board of directors and take minutes of the discussions and decisions taken at any such meetings. (May be different to a secretary who is an officer.)
- Committee chairs – directors may serve as chairs of various board committees, such as the Audit Committee, Compensation Committee and Nominating Committee. Committee chairs are responsible for leading committee meetings, overseeing specific areas of corporate governance and making recommendations to the full board.

4.3 Board Composition Requirements/Recommendations

The only requirement is that directors be natural persons of legal age. There are no composition requirements, such as regarding independent directors, etc.

4.4 Appointment and Removal of Directors/Officers

The members of the board of directors of a corporation are elected annually by a majority vote of the shareholders present at the annual meeting of shareholders, in person or via proxy, who have the right to vote at such meeting. It is important to note that the certificate of incorporation may provide for the creation of a staggered board with two or three groups of directors, who may serve for a period of one to three years. In a staggered board, only one group of directors will be elected at each annual meeting of shareholders. Through its articles of incorporation and/or its by-laws, a Puerto Rico Corporation may establish other restrictions or requirements for directors.

In a non-staggered board of directors, any one director or the whole board of directors may be removed with or without cause by the holders of a majority of the shares entitled to vote for the election of directors.

In a staggered board of directors, shareholders may only remove a director for just cause, unless otherwise provided in the certificate of incorporation. Furthermore, if the certificate of incorporation authorises cumulative voting, no director may be removed if the cumulative votes against their removal are sufficient to elect such director as a member of the board of directors.

In the event of a vacancy as a result of the removal, resignation or death of a director, the remaining members of the board of directors

may designate a director without seeking the approval of the shareholders. A director designated to the board of directors in such a fashion shall serve for the remainder of the former director's term.

Unless otherwise specified in the certificate of incorporation or by-laws, the officers of a corporation are appointed by the board of directors without the need to seek the consent of the shareholders. The board of directors has the exclusive power to appoint and remove corporate officers as they deem to be in the best interests of the corporation.

The members of an LLC may choose to appoint a manager or a group of managers who will have the rights and responsibilities provided in the limited liability company agreement. The authors note that the Corporations Act does not directly address the removal of the manager of an LLC; however, a manager may be removed by the members holding a majority interest in the LLC.

4.5 Rules/Requirements Concerning Independence of Directors

Although there are no legal requirements for Puerto Rico corporations to have an independent director(s), under the Corporations Act, independent directors are considered objective and free from conflicts of interest that could compromise their judgement, and there are rules and requirements related to the independence of directors and the management of potential conflicts of interest. These rules aim to ensure that directors act in the best interest of the corporation and its shareholders. Among the most salient key considerations are the duty of loyalty and the duty of care, which are discussed in further detail in 4.6 Legal Duties of Directors/Officers.

4.6 Legal Duties of Directors/Officers

The directors and officers of a corporation are bound by three principal legal obligations:

- to act pursuant to the objectives and purposes of the corporation;
- to perform their duties with the care and attention that a reasonable and competent person would exercise under similar circumstances ("*duty of care*") and
- to act in a just manner and exercise their powers with the utmost loyalty and in the best interests of the corporation and its shareholders ("*duty of loyalty*").

The duty of care includes responsibilities such as:

- the duty to monitor; and
- the duty to make enquiries.

The duty of loyalty imposes upon directors and officers the obligation to act in the best interest of the corporation and its shareholders, setting aside their own personal interests. In order to comply with this duty of loyalty, the directors and officers must avoid transactions that may result in a conflict of interest with the corporation. The directors and officers of a corporation should not engage in or become involved with businesses that compete with the corporation, nor should they use material non-public information for their personal gain.

The Corporations Act expressly extends the duties set forth above to the members and managers of LLCs.

A director will be found to have violated their duty of care where a plaintiff is able to prove that the actions of the director were grossly negligent. To establish that the director was grossly

negligent, the plaintiff must first overcome the presumption provided by the “*business judgement rule*” ie, the presumption that in making a decision, the director was informed and acted in good faith and in what they believed were the best interests of the corporation.

Furthermore, the business judgement rule provides that the plaintiff must prove that a reasonable commercial basis for the director’s decision did not exist. The underlying purpose of the business judgement rule is to allow directors and officers to make reasonable business decisions without holding them responsible for the success or failure of each venture.

Where the presumption established by the business judgement rule is overcome, the implicated directors are subject to the “*entire fairness*” judicial standard of review, under which a director must show that the decision was taken with the utmost good faith and that it was inherently fair to the shareholders.

Notwithstanding the foregoing, a corporation’s certificate of incorporation may include a provision limiting or eliminating the monetary responsibility of a director or officer for breaching their fiduciary duties, with the exception of the duty of loyalty and acts or omissions done in bad faith.

4.7 Responsibility/Accountability of Directors

Fiduciary duties are owed to the corporation and shareholders. In the case of LLCs, members and managers are subject to the same fiduciary duties as the directors, officers and shareholders of a Puerto Rico Corporation.

Regularly, in terms of fiduciary duties, the board or management body is required to take into consideration the interests of the entity itself and of

its shareholders or members. That said, through the certificate of incorporation or by-laws (for corporations), and especially in the limited liability company agreement (for LLCs), other interests may be agreed upon for consideration by the board or management body. As previously mentioned, in the case of a Benefit Corporation, directors, in making their determinations, are allowed to consider factors other than the best interests of the shareholders; for example, they are allowed to take into consideration the general public benefit being pursued, the best interests of the employees and the community at large (among other things).

4.8 Consequences and Enforcement of Breach of Directors’ Duties

Excluding derivative suits, shareholders may bring a direct lawsuit against directors and officers if they can demonstrate that they suffered harm individually as a result of the breach of fiduciary duties. This typically requires a showing of personal loss or injury separate from the harm suffered by the corporation as a whole. The responsible directors and officers can be held liable for their breach of fiduciary duties through various means, which may include the following.

- Monetary damages – directors and officers found to have breached their fiduciary duties can be held personally liable for monetary damages. This may include compensating the corporation, shareholders or other affected parties for any financial losses incurred as a result of the breach.
- Injunctive relief – courts can issue injunctions to prevent the continuation of the wrongful conduct or to require specific actions to rectify the breach and protect the interests of the corporation or affected parties.
- Rescission or restoration – in cases where the breach involved a transaction or action that

harmed the corporation or its stakeholders, the court may order the rescission or undoing of the transaction or the restoration of the corporation to its prior condition.

- Removal or disqualification – in extreme cases of breach of fiduciary duties, the court may even order the removal of directors or officers from their positions.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

See 4.6 Legal Duties of Directors/Officers. Breaches of the limited liability company agreement by a member or manager may also be enforced against them.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

The Corporations Act does not impose any limitations on the compensation of directors. Unless otherwise specified in the certificate of incorporation or the by-laws, the board of directors has the authority to determine the compensation to be paid to the officers and directors of the corporation. The Corporations Act does not specifically address this matter in connection with LLCs.

4.11 Disclosure of Payments to Directors/Officers

See 4.10 Approvals and Restrictions Concerning Payments to Directors/Officers.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Except for certain extraordinary matters (such as a merger or consolidation, conversion, the sale of all or substantially all of the assets, or dissolu-

tion) for which shareholder approval is required, generally shareholders do not have corporate governance responsibilities in corporations.

Notwithstanding the foregoing, in situations where a majority shareholder has a conflict of interest with respect to a corporate matter, the Corporations Act imposes upon the controlling shareholder a duty of loyalty. In the case of LLCs, the Corporations Act establishes that members are bound by the same duty of loyalty to the LLC and to the other members as established for directors, officers and shareholders of a corporation. For LLCs, the Corporations Act allows for different responsibilities to be agreed upon in the limited liability company agreement.

5.2 Role of Shareholders in Company Management

One of the basic tenets of corporate law under the Corporations Act is that the business of a corporation shall be managed by or under the direction of a board of directors. Thus, shareholders are generally not involved in the direct management of the corporation. The principal exception to this occurs in the context of close corporations, in which the shareholders may be primarily responsible for the operation and management of the entities, if such governance structure is so provided for in the articles of incorporation.

Nonetheless, shareholders have the right and the power to elect the board of directors, as well as the right to vote on and approve extraordinary transactions, such as:

- any amendment to the certificate of incorporation or the by-laws;
- a merger, consolidation or conversion;
- the sale of all or a substantial amount of the assets of the corporation; or

- a dissolution.

Contrary to corporations, LLCs are regularly managed in a decentralised fashion by their members (similar to partnerships) and members actively participate in the operation and management of the LLC. The Corporations Act provides that unless otherwise established in the limited liability company agreement, the LLC will be managed by the members owning more than 50% of the equity interests in the LLC.

Notwithstanding the foregoing, the members may choose to implement a centralised management structure, similar to that of a corporation, including the election of a board of managers and the appointment of officers. In such case, the members need to specify in the LLC's limited liability company agreement the particular requirements regarding the management structure, including what rights they wish to retain for themselves and wish to not delegate to the LLC's board of managers and officers.

5.3 Shareholder Meetings

The Corporations Act requires that corporations hold an annual meeting of shareholders, and allows the board of directors to convene special meetings of shareholders to discuss and take action on particular matters. The Corporations Act further provides that the notification period for an annual or special meeting must be no less than ten days and no more than 60 days prior to such meeting. If the notification is for a special meeting, the purpose of that meeting must also be disclosed in the notification.

In addition, the by-laws of the corporation may establish additional rules regarding who may convene special shareholder meetings. For example, they could provide that the shareholders holding a majority of the voting rights may

convene a special meeting. In annual and special meetings, the shareholders have the right to vote (either in person or via proxy) on the matters brought before them. The Corporations Act also allows for participation via electronic methods.

Contrary to corporations, LLCs are not statutorily required to hold annual or special member meetings; thus, the establishment of such meetings and the rules governing them are subject to the discretion of the members or as otherwise stated in the limited liability company agreement.

5.4 Shareholder Claims

A shareholder may present a direct action against the corporation and its management alleging that they have suffered damages as an individual shareholder.

Additionally, shareholders (and, in certain situations, creditors) may pursue derivative actions against management. In a derivative action, a shareholder or group of shareholders pursues a claim on behalf of the corporation where the directors or officers of the corporation fail to do so or violate one or more of their fiduciary duties. This inaction on the part of management typically takes place where the directors or officers of the corporation are responsible for the damages alleged under the derivative action.

It is important to note that under a derivative action, any relief or award granted by the courts shall be for the sole benefit of the corporation and not of the shareholder(s) who initiated the action. In the case of an LLC, the Corporations Act expressly states that only a current member of the LLC may file a derivative suit.

5.5 Disclosure by Shareholders in Publicly Traded Companies

See 1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

There is no statutory requirement for private companies regarding corporate governance disclosures to private parties, besides compilation of the company's organisational documents (such as the certificate of incorporation and by-laws), the shareholders' agreement (if adopted), the certificate of organisation and the limited liability company agreement, available to the shareholders and members of the corporation and/or LLC. See also 7. Audit, Risk and Internal Controls.

However, the Corporations Act requires that all corporations file an annual report to the Puerto Rico Department of State, detailing, among other things, the identity of at least two officers and/or directors of the corporation. The Corporations Act does not require such disclosure for LLCs with the Puerto Rico Department of State. Such annual reports are available to the public through the Department of State's website. However, no other requirement for public disclosure on websites exists in Puerto Rico.

6.2 Disclosure of Corporate Governance Arrangements

See 6.1 Financial Reporting.

6.3 Companies Registry Filings

In addition to annual reports as discussed in 6.1 Financial Reporting, corporations and LLCs

have to register the following with the Puerto Rico Department of State:

- the certificate of incorporation or organisation; and
- amendments, mergers, consolidations and dissolutions.

Additionally, corporations and LLCs are now obligated to file their existence or dissolution with the Registry of Legal Entities. Such filings, including annual reports, are publicly available.

Failure to make such filings would result in such acts being regarded as having not taken place. Not presenting the annual reports or not paying annual dues may result in the cancellation of the entity.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Under the Corporations Act, corporations with an annual business volume in excess of USD3 million are required to file with the Puerto Rico Department of State an audited balance sheet, together with their annual report. LLCs are not required to file financial reports with the Puerto Rico Department of State.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Under Delaware case law, which, as previously indicated, is highly persuasive in Puerto Rico, directors have certain requirements and responsibilities regarding risk management and internal controls.

While Delaware courts generally afford directors considerable discretion in managing the affairs

of the corporation pursuant to the business judgement rule, directors are expected to fulfil their duties of care and loyalty, which encompass risk oversight and internal controls. This involves:

- understanding and assessing the major risks the corporation faces;
- ensuring that appropriate risk management and internal control systems are in place; and
- periodically reviewing the effectiveness of these systems.

Internal controls are systems, processes and policies designed to:

- safeguard the corporation's assets;
- promote accurate financial reporting; and
- ensure compliance with applicable laws and regulations.

SENEGAL



Law and Practice

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Houda Law Firm was founded in 1977 in Dakar, Senegal, and consists of a 70-person staff – half of whom are specialised and highly qualified lawyers and legal advisers working to assist clients (such as private companies, public entities and individuals) with all their legal needs in Senegal and the West African Economic and Monetary Union (WAEMU) member states. The

firm opened a branch in Abidjan, Côte d'Ivoire, in 2018, which made it the first foreign law firm from the WAEMU region to be established in the country. The team works on matters related to company incorporation, investment, employment law, taxation, business litigation, and arbitration. Houda Law Firm was certified in September 2020 (ISO 9000-2015).

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Commercial companies are governed in Senegal by the Uniform Act on Commercial Companies and Economic Interest Groups (*Acte Uniforme révisé relatif au droit des Sociétés Commerciales et du Groupement d'Intérêt Économique*, or AUSCGIE), published on 30 January 2014. The most commonly used commercial forms are, in order, the *société à responsabilité limitée* (SARL), the *société anonyme* (SA) and the *société par actions simplifiée* (SAS).

SARL

The SARL the simplest of commercial companies, in which the liability of the shareholders is limited to contributions. A SARL may be established by one natural or legal person or between two or more natural or legal persons. A SARL does not require any minimum share capital for its creation, and its capital is divided into shares.

The SARL is often characterised by a fairly strong *intuitu personae*, which is why transfers of shares are often governed by specific authorisation rules given by the non-transferring shareholder. The SARL is managed by one or more natural persons, associated or not.

In addition, a SARL is not required to appoint an auditor unless it meets two of the following conditions at the end of the financial year:

- a balance sheet total exceeding XOF125 million;
- an annual turnover exceeding XOF250 million; and/or
- a permanent staff of more than 50 persons.

The shareholders of the SARL meet in a general meeting, either ordinary (each year for the approval of the accounts of the closed financial year) or extraordinary (for any modification of the articles of association).

The SARL is a suitable corporate structure for greenfield projects, commercial activities and services. It is also suitable for young entrepreneurs with few resources, due to its low formation cost.

SA

The SA under the AUSCGIE may be held by a single shareholder. In terms of management and administration, the founder(s) must choose unequivocally in the articles of association between:

- an SA with a board of directors (one shareholder or more); or
- an SA with a managing director (up to three shareholders).

The minimum share capital of an SA is XOF10 million. It must be fully subscribed by the shareholders and at least one quarter of the total share capital must be paid up at the time of incorporation.

The founders of an SA must appoint a statutory auditor and an alternative auditor, chosen from among experts who are members of the National Institute of Chartered Accountants of Senegal (*Ordre National des Experts Comptables et Comptables Agréés du Sénégal*, or ONECCA).

SA with a board of directors

The board of directors is composed of a minimum of three persons and a maximum of 12 members, shareholders or not. The articles of association may require each director to own a number of shares of the company over which

they preside. It is possible to appoint corporate directors, who appoint a permanent representative to the board.

The board appoints the chairperson of the board of directors from among the natural persons who are members of the board and also appoints the CEO of the company, who may be one third of the board. It may also be decided to appoint a chairperson and CEO who will combine both roles.

The board of directors determines the company's strategic objectives and ensures their implementation. It controls and verifies the proper functioning of the company and settles matters regarding the company through its deliberations. The chair of the board of directors presides over board meetings and general meetings. The chairperson must ensure that the board assumes control of the management of the company, which is entrusted to the CEO under the board's oversight.

The CEO is responsible for the general management of the company and represents the company in its relations with third parties. At the suggestion of the CEO or the chairperson/CEO, the board of directors may appoint one or more individuals to assist the CEO or the chairperson/CEO as deputy CEO.

The SA with a managing director (administrateur général)

The managing director assumes responsibility for the administration and general management of the company. They represent it in its relations with third parties and convene and chair the general meetings of shareholders. The managing director is vested with the broadest powers to act in all circumstances on behalf of the company but must exercise these powers within

the limits of the corporate purpose and subject to those powers expressly attributed to shareholders' meetings by the AUSCGIE and, where applicable, by the articles of association.

At the suggestion of the managing director, the general meeting may mandate one or more deputy managing director(s) to assist the director, as well as decide other powers delegated to the deputy managing director.

The SA is a suitable form of company for the establishment of joint ventures, for companies with significant investments to make, and for companies engaged in regulated banking or financial activities.

SAS

Introduced in the AUSCGIE in 2014, the SAS is a company set up by one or more shareholders where the articles of association determine the organisation and operation of the company, subject to certain mandatory rules (eg, competence of the shareholders' general meeting to approve the accounts or amend the articles of association).

The liability of the shareholders is limited to the contributions and there is no minimum share capital required to create an SAS. When created by a single shareholder, it is called a single-person simplified joint stock company (*société par actions simplifiée unipersonnelle*, or SASU).

The company is represented by a chairperson, appointed under the conditions provided for in the articles of association. The chairperson is vested with the broadest powers to act on behalf of the company within the limits of the corporate purpose.

The articles of association freely determines the decisions that must be taken collectively by the shareholders and stipulate the conditions and forms in which the shareholders must take these decisions. Decisions taken in violation of the statutory clauses are null and void.

The appointment of one or more auditors is optional unless the SAS meets two of the following conditions at the end of the financial year:

- a balance sheet total exceeding XOF125 million;
- an annual turnover exceeding XOF250 million; and/or
- a permanent workforce of more than 50 people.

An SAS that controls or is controlled by one or more companies is also required to appoint at least one auditor.

This form of commercial company is appropriate for companies with diverse shareholder profiles – ie, particularly where investors and project leaders, equity companies, and companies operating in the field of services and new technologies are among the company's shareholders.

1.2 Sources of Corporate Governance Requirements

As Senegal is a member state of the Organisation for the Harmonisation of Business Law in Africa (*Organisation pour l'Harmonisation en Afrique du Droit des Affaires*, or OHADA), company law in Senegal is subject to OHADA law – more specifically, to the AUSCGIE. The articles of association and the shareholders' agreement are also sources of corporate governance.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies making a public offering of their shares in one or more OHADA contracting states or whose shares are listed on the stock exchange of one or more OHADA contracting states are required to have a board of directors. The boards of directors of the companies must be composed of at least three members and at most 15 members at the time a company's shares are admitted to the stock exchange.

However, in the event of a merger involving one or more companies whose shares are admitted to the stock exchange of one or more “party states”, the number of members may exceed 15 (up to the total number of directors who have been in office for more than six months in the merged companies) but may not exceed 20. When the shares of the company are admitted to the stock exchange of one or more of the state parties, no new directors may be appointed – nor may directors who have died or ceased to hold office be replaced – until the number of directors has been reduced to 15. If a company admitted to the stock exchange of one or more party states is delisted from that stock exchange, the number of directors must be reduced to 12 as soon as possible.

Within the various limits set out here, the number of directors is freely determined in the articles of association.

The board of directors of the company is obliged to have an audit committee (*comité d'audit*). The audit committee is composed exclusively of directors who are not employees of the company or who do not hold a position as chairperson/CEO, CEO or deputy CEO within the company. The board of directors ensures the competence

of the directors it appoints to the audit committee.

The main tasks of the audit committee are to:

- review the accounts and ensure the relevance and consistency of the accounting methods used to prepare the company's consolidated and parent-company financial statements;
- monitor the process of preparing financial information;
- monitor the effectiveness of internal control and risk management systems;
- issue an opinion on the auditors proposed for appointment by the general meeting; and
- report regularly to the board of directors on the performance of its duties and inform the board of directors without delay of any difficulties encountered.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

The Ministerial Order of 2 September 2022 specifying the modalities of identification, declaration, conservation and control of information on beneficial owners imposes on legal persons and legal arrangements (ie, trusts and fiduciaries):

- an obligation to identify beneficial owners and to keep a register of beneficial owners; and
- an obligation to declare to the tax authorities information on beneficial owners.

It is mandatory to file declarations with the tax authorities:

- on the creation of the taxable person;
- on the anniversary of its incorporation (for those not subject to income tax); and

- within 15 days of an event making it necessary to modify the information on the beneficial owners (eg, death, transfer of shares).

A [platform](#) has been deployed to enable taxpayers to comply with their obligations.

Any failure to comply with the above-mentioned provisions is effectively sanctioned by a fine of XOF1 million due as many times as there are documents or information that is either:

- requested and not produced; or
- omitted, incomplete or inaccurate.

2.2 ESG Considerations

There are no regulations on ESG issues in OHA-DA law. These provisions will, for example, be provided for by the board of directors or provided for by the internal regulations on a case-by-case basis for companies that can draw on international regulations in this area.

In specific sectors such as extractive industries, the most recent legislations impose transparency obligations with regard to revenues paid to the state.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

In general, in commercial companies:

- the management body, the officers, and the board have – within the time limits set forth in the AUSCGIE for each type of company – full powers to bind the company towards third parties without having to produce a special power of attorney and any limitations on their legal powers by the articles of association

will be unenforceable against bona fide third parties; and

- the company is bound by acts of its management body, its officers and its board that are not within the company purpose, unless the company can prove that the third party was aware that the act was unrelated to that purpose or could not ignore this given the circumstances – although the mere publication of the articles of association is not enough to prove it.

SARL Management

A SARL is managed by one or more managers (*gérants*), who must be natural persons. Managers may or may not be shareholders of the company. The managers are appointed by the shareholders in the articles of association or by a decision of the shareholders' general meeting. In the absence of specific provisions in the articles of association, the manager(s) is (are) appointed for four years and are re-electable. There are no nationality or residence requirements for managers.

SA Management

The articles of association must specify under which of the following management structures the SA will be managed:

- a board of directors with a single chairperson and general manager (*président-directeur général*), who must be a director of the company and a natural person; or
- a board of directors with a chairperson of the board and a separate general manager (*directeur général*), who must be a natural person but does not have to be a director of the company and who may be assisted by one or more assistant general managers.

In both of these scenarios, directors may or may not be shareholders of the company, unless provided for in the articles of association. The board must have at least three and no more than 12 directors.

Companies having fewer than three shareholders may choose not to form a board of directors and instead to appoint a general manager (*administrateur général*, who may or may not be a shareholder of the company) who will be responsible for the administration and direction of the company.

SAS Management

An SAS is represented towards third parties by a president, who may be a natural or legal person and who may or may not be a shareholder of the company. The articles of association may provide for the conditions under which one or more individuals other than the president, with the title of general manager or deputy general manager, may exercise the powers entrusted to them by the articles of association. Restrictions on the powers of the president, general manager or deputy general manager, as detailed in the provisions of the articles of association and the decisions of legal representatives, are not enforceable against third parties.

It is also possible for an SAS to set up a board of directors.

3.2 Decisions Made by Particular Bodies SARL Decision-Making

In relation to the shareholders and in the absence of determination of the manager's powers by the articles of association, the manager may carry out all acts of management in the interest of the company. Where there is more than one manager, they shall hold separately the powers provided for in the articles of association, except

for the right of each of them to object to any transaction before it is concluded. Opposition by one manager to the acts of another manager is without effect with regard to third parties, unless it is established that the third parties have knowledge of it.

SA Decision-Making

SA with a board of directors

The board of directors determines the SA's strategic objectives and ensures their implementation. Within the limits of the company's purpose and subject to any decision-making powers expressly delegated to the shareholders' meetings, the board of directors deals with any issue concerning the proper operation of the company and – through the board members' deliberations – settles matters that concern the SA.

The board of directors carries out any such controls and verifications as it deems appropriate. The board of directors may entrust one or more of its members with special mandates for one or more specific purposes.

The chairperson of the board of directors chairs the meetings of the board of directors and the general meetings. The chairperson must ensure that the board of directors assumes the control of the management of the company, which is entrusted to the general manager. At any time, the chairperson of the board of directors may carry out the verifications the chairperson deems appropriate and may obtain from the general manager – who is obliged to comply – all the documents the chairperson deems useful for the accomplishment of that purpose.

The general manager is responsible for the general management of the company. They represent the company in its relations with third parties.

SA with a managing director

The managing director is responsible for the administration and general management of the company. They represent the company in its relations with third parties, and convene and chair the shareholders' meetings. The managing director is vested with the broadest powers to act in all circumstances in the name of the company but must exercise them within the limits of the corporate purpose and subject to those powers expressly conferred on shareholders' meetings by the AUSCGIE and, where applicable, by the articles of association.

Meetings in the SA

Extraordinary general meeting

The extraordinary general meeting is the only body empowered to modify the statutes in all their provisions. The extraordinary general meeting is also competent to:

- authorise mergers, demergers, transformations and partial contributions of assets;
- transfer the registered office to any other city of the OHADA contracting state where it is located or to the territory of another state; and
- dissolve the company early or extend its term (see **5.3 Shareholder Meetings**).

Special meeting

The special meeting brings together the holders of shares of a given category. The special meeting approves or disapproves the decisions of the general meetings when these decisions modify the rights of its members.

Ordinary general meeting

The ordinary general meeting takes all decisions other than those expressly reserved for extraordinary general meetings and those reserved for

special meetings (see **5.2 Role of Shareholders in Company Management**).

SAS Decision-Making

The SAS is a company set up by one or more shareholders and whose articles of association freely provides for the organisation and operation of the company. The company is represented with regard to third parties by a president appointed under the conditions provided for by the articles of association. The president is vested with the broadest powers to act in all circumstances on behalf of the company, within the limits of the corporate purpose. The articles of association may provide for the conditions under which one or more persons other than the president, bearing the title of chief executive officer or deputy chief executive officer, may exercise the powers conferred on the latter by the articles of association.

The articles of association determines the decisions that must be taken collectively by the shareholders and stipulate the forms and conditions in which the decisions must be taken. However, the powers vested in the extraordinary and ordinary general meetings of joint stock companies are – under the conditions stipulated by the articles of association – exercised collectively by the shareholders in matters of:

- increase, amortisation or reduction of capital;
- merger;
- demerger;
- partial contribution of assets;
- dissolution;
- transformation into a company of another form;
- appointment of auditors;
- annual accounts; and
- profits.

3.3 Decision-Making Processes

Decisions are taken by general meetings, which may be ordinary or extraordinary, and which decide according to the majority and quorum rules set out in the AUSCGIE or – in the case of the SAS – in the articles of association. These rules differ according to the corporate form (see **5.3 Shareholder Meetings** for the majority and the type of decision). The general meetings are convened by the corporate representatives, following a formal procedure prescribed by the AUSCGIE.

The shareholders are convened at least 15 days before the meeting by hand-delivered letter against a receipt, or by registered letter with a request for acknowledgement of receipt, or by fax or email. The notice of meeting indicates the date, place and agenda of the meeting. The meeting cannot deliberate on a question that is not registered on its agenda.

These decisions of the shareholders must be recorded in the minutes, which indicate the date and the place of the meeting, the names and first names of the shareholders present, the agenda, the documents and reports submitted for discussion, a summary of the debates, the text of the resolutions put to the vote, and the results of the votes.

4. Directors and Officers

4.1 Board Structure

An SA may be managed by a board of directors consisting of at least three and not more than 12 members, who may or may not be shareholders. The articles of association may require that each director own a number of shares in the company for which they make determinations. This provision shall not apply in the case of employees

appointed as directors. Every director must, on the day of their appointment, hold the number of shares required by the articles of association or during their term of office.

In the case of an infringement, the director must resign from their office within three months of their appointment or - if the infringement occurs during their term of office – within three months of the date of the transfer of shares giving rise to the infringement. At the end of this period, the director shall be deemed to have resigned from their mandate and must return the remuneration received (in whatever form) without the validity of the deliberations in which they took part being called into question.

The auditors exercise a supervisory role and must disclose any violations in their report to the annual general meeting. The first directors are appointed by the articles of association or, where appropriate, by the constituent general meeting.

During the life of the company, the directors shall be appointed by the ordinary general meeting. However, in the event of a merger, the extraordinary general meeting may appoint new directors.

Any appointment made in violation of the provisions of the articles of association is null and void. The term of office of the directors is freely determined by the articles of association, but may not exceed six years in the case of appointment during the life of the company and two years in the case of appointment by the articles of association or by the constituent general meeting.

4.2 Roles of Board Members

The board of directors determines the company's strategic objectives and ensures their

implementation. The board of directors has a chairperson and may entrust one or more of its members with special mandates for one or more specific purposes.

4.3 Board Composition Requirements/Recommendations

The choice of directors is freely determined by the shareholders. There is no longer a quota rule to be respected between the number of shareholder and non-shareholder directors, as was the case with the pre-2014 AUSCGIE. However, the articles of association may require that each director own a number of shares of the company for which they make decisions. In practice, the composition of the board of directors often mirrors the composition of the company's shareholding.

4.4 Appointment and Removal of Directors/Officers

The directors or officers are appointed by the articles of association at the time of the company's incorporation, or during the company's life, by the general meeting. The terms of appointment, re-election, replacement and dismissal are freely determined by the articles of association. The directors may be re-elected unless the articles of association states otherwise. In an SA, the duration of office of the president and managing director is aligned with that of the directors. The termination of the functions of the directors must be published in the commercial register.

4.5 Rules/Requirements Concerning Independence of Directors

Two mechanisms are provided for by the AUSCGIE to prevent conflicts of interest between the company and its directors.

The Rules of Non-Cumulation of the Roles of Legal Representatives (in an SA)

For directors (in an SA with a board of directors)

Subject to certain reservations, a natural person – either directly or as a permanent representative of a legal entity director - may not simultaneously belong to more than five boards of directors of SA companies that have their registered office in the territory of the same state party. Any natural person who, upon taking up a new term of office, finds themselves in breach of this rule must resign from one of their terms of office within three months of their appointment.

For the president and managing director

No person may simultaneously hold more than three offices as president and managing director of an SA that has its registered office in the territory of the same party state.

Likewise, the role of president and managing director may not be held concurrently with more than two roles as general director or general manager of an SA that has its registered office in the territory of the same contracting state. Any natural person who, upon taking up a new term of office, finds themselves in breach of this rule must resign from one of their terms of office within three months of their appointment.

For the general director

No person may simultaneously hold more than three offices as a general director of corporations that have their headquarters in the territory of the same state party. Similarly, the office of general director may not be held concurrently with more than two offices of president and general manager or general manager of an SA which has its registered office in the territory of the same contracting state. A director who, upon taking up a new term of office, is in violation of this rule

must, within three months of their appointment, resign from one of their offices.

Procedure for Regulated Agreements (in an SARL, an SA and an SAS)

According to Article 438 of the AUSCGIE, the following agreements must be subject to prior authorisation by the board of directors of an SA:

- any agreement between the SA and one of its directors, general managers or assistant general managers;
- any agreement between a company and a shareholder who holds 10% or more of the company's capital;
- any agreement in which a director, general manager, deputy general manager or shareholder with a holding of 10% or more of the company's capital is indirectly interested or in which they deal with the company through an intermediary; and
- any agreement between a company and a business or legal entity, if one of the directors, the general manager, the assistant general manager or a shareholder holding a stake equal to or greater than 10% of the company's capital is an owner of the business or an indefinitely liable shareholder, manager, director, general manager, assistant general manager, general manager, assistant general manager or other corporate officer of the contracting legal entity.

Similar provisions are provided for the SARL and the SA; regulated agreements must be approved by the ordinary general meeting (Articles 350 and 853-14 of the AUSCGIE).

4.6 Legal Duties of Directors/Officers

There are no specific provisions in the law regarding the principal legal duties of the directors and officers of a company. However, Article

480, Section 2 of the AUSCGIE provides that the chairperson must ensure that the board of directors assumes control of the management of the company, which is entrusted to the general manager. Thus, the chairperson and the board of directors each have a role.

4.7 Responsibility/Accountability of Directors

SARL Managers

The managers will be liable – individually or jointly and severally – as the case may be, to the company or to third parties, either:

- for infringements of the legal or regulatory provisions applicable to private limited companies;
- for breaches of the articles of association; or
- for faults committed in their management.

If several managers have co-operated in the same acts, the competent court determines the contributory share of each of them in the remedy of the damage (Article 330 of the AUSCGIE).

SA Directors

The directors will be individually or jointly and severally liable to the company or to third parties, either for infringements of the legal or regulatory provisions applicable to an SA, or for violations of the provisions of the articles of association, or for faults committed under their management.

Where several directors have co-operated in the same acts, the competent court will determine the contributory share of each of them in the remedy of the damage (Article 740 of the AUSCGIE).

In an SAS

The rules governing the liability of the members of the board of directors of an SA are applicable

to the chairperson and the officers of an SAS (Article 853-10 of the AUSCGIE).

4.8 Consequences and Enforcement of Breach of Directors' Duties

Liability Actions

Two types of actions are provided for by the AUSCGIE.

Individual action

Pursuant to Articles 161 et seq of the AUSCGIE, third parties or shareholders may take individual action to hold a corporate officer liable for misconduct in the performance of their duties, without prejudice to the company's potential liability. If several corporate officers have participated in the same acts, they are jointly and severally liable to third parties.

This individual action is an action for damages suffered by a third party or by a shareholder, where the latter suffers a loss distinct from the loss suffered by the company, as a result of a fault committed individually or collectively by the corporate officers or directors in the exercise of their duties.

This action is brought by the person who suffers the damage.

Corporate action (action sociale) – Articles 165 et seq of the AUSCGIE

A corporate action is an action for compensation for the damage suffered by the company as a result of a fault committed by corporate officer(s) in the performance of their duties. The corporate action filed against one or several corporate officers can be initiated either by the company itself (through the other officers who are not involved) or by one or several shareholders in the case of failure of the competent bodies. The corporate action is reserved only for the sharehold-

ers holding shares on the day it is implemented and who retain the status of shareholder during the whole duration of the procedure.

In the case of a SARL, Article 331 of the AUSCGIE provides that several shareholders may only claim compensation for the damage suffered by the company if they represent one quarter of the shareholders and one quarter of the company shares. These two conditions are cumulative. However, in the case of an SA, the shareholders can only exercise the corporate action if they represent at least one twentieth of the share capital (Article 741 of the AUSCGIE).

The individual and corporate action can be triggered and acted upon concurrently/simultaneously.

Grounds for Liability

A breach of directors' duties would give rise to their liability. Similar provisions govern the rules pertaining to the liability of corporate officers and directors in the different types of companies that have been described: SARL, SA and SAS. A distinction must be made between civil and criminal liability.

Civil liability of the manager of a SARL and the directors of an SA

The liabilities are similar for the manager of a SARL and the directors of an SA. They are liable – individually or jointly and severally, as the case may be – to the company or to third parties, either for breaches of the laws or regulations applicable to companies, or for breaches of the articles of association, or for misconduct in their management. If several managers or directors have co-operated in the same acts, the competent court will determine the contribution of each of them to the compensation for the damage.

In addition to the action for compensation for the damage suffered personally, the shareholders representing one quarter of the shareholders and one quarter of the shares may – either individually or by grouping together – proceed with the social action for liability against the manager or director(s). No clause in the articles of association may make the exercise of the corporate action subject to the prior notice or authorisation of the meeting or entail a waiver in advance of the exercise of this action.

No decision of the meeting may have the effect of extinguishing an action for liability against the managers for misconduct committed in the performance of their duties. Any decision to the contrary is null and void.

Civil liability of the CEO of an SA

The same rules of individual and social responsibility apply to the CEO.

Civil liability of the directors of an SA

Directors are individually or jointly and severally liable to the company or to third parties, either for breaches of the laws or regulations applicable to an SA, or for breaches of the provisions of the articles of association, or for misconduct in their management.

Civil liability of the president/chairperson of an SAS

The same rules of individual and social responsibility as those mentioned for the manager and the CEO apply to the president.

Criminal liability

The AUSCGIE contains criminal provisions in the event of offences committed by corporate officers:

- the incorporation of companies;

- the management, administration and direction of the company;
- general meetings;
- changes in the capital of an SA, capital reductions;
- company control;
- dissolution of companies;
- liquidation of companies; and
- in the event of a public offering for savings.

Law No 2018-13 of 27 April 2018 describes the penalties incurred for the offences referred to in the AUSCGIE.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Other bases for claims or enforcement against directors or officers for breaches of corporate governance requirements that exist in Senegal are as follows.

Management Expertise

Pursuant to Article 159 of the AUSCGIE, one or more shareholders representing at least one tenth of the share capital may - either individually or by grouping together in any form whatsoever – request the competent court of the registered office, ruling within a short period of time, to appoint one or more experts to present a report on one or more management operations.

Provisional Administration

When the normal functioning of the company is made impossible, either because of the management, executive or administrative bodies or because of the shareholders, the competent court – ruling within a short period of time – may decide to appoint a provisional administrator for the purpose of temporarily managing the company's affairs (Article 160-1 of the AUSCGIE).

Given that - according to the general law of civil liability - the potential liability of directors is likely to be implemented as soon as it can be established that they have committed errors in the performance of their duties and that these errors have had harmful consequences for the company, the shareholders or third parties, the liability of a director or officer can only be limited by proving that the damage results either from a force majeure or from a fault of the victim or of a third party.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Article 325 of the AUSCGIE

In a SARL, the duties of a manager may be performed free of charge or with remuneration, under the conditions laid down in the articles of association or in a collective decision of shareholders. The manager, when a shareholder, does not take part in the vote on the deliberation relating to their remuneration and their votes shall not be taken into account for the calculation of the majority. Any deliberation taken in violation of Article 325 of the AUSCGIE is void. The determination of the remuneration is not subject to the regime of related-party agreements.

In an SA, the ordinary general meeting may allocate to the directors – as remuneration for their activities – a fixed annual sum that it determines at its own discretion (commonly called “*jetons de présence*” in French).

Unless otherwise provided for in the articles of association, the board of directors is free to allocate the compensation among its members. The board of directors may also allocate to its members exceptional remuneration for the missions and mandates entrusted to them or authorise the reimbursement of travel expenses and expenses

incurred in the interest of the company, subject to the provisions concerning regulated agreements.

A director may enter into an employment contract with the company if that contract corresponds to actual employment. Apart from sums received under an employment contract, the directors may not receive – in respect of their duties – any other remuneration (permanent or otherwise) than that provided for by the board of directors (Articles 430, 431 and 432 of the AUSCGIE).

The CEO may be bound to the company by a contract of employment. The terms and amount of the remuneration of the chairperson and managing director are fixed by the board of directors. Where necessary, the benefits in kind granted to them are fixed in the same manner as their remuneration. The CEO may not receive any other remuneration from the company (Article 466 of the AUSCGIE).

In an SAS, the remuneration and benefits of the chairperson and of the potential other directors are determined by the articles of association and the shareholders.

4.11 Disclosure of Payments to Directors/Officers

No public disclosure obligations in relation to the remuneration, fees or benefits payable to directors and officers for companies have been identified, except for publicly traded companies. Indeed, Article 831-2 of the AUSCGIE requires the disclosure of the report prepared by the chairperson of the board of directors containing – in addition to the composition of the board of directors and its operating conditions – the compensation allocated to the corporate officers.

Regarding other disclosures, pursuant to Article 432 of the AUSCGIE, the exceptional remuneration of directors for missions and mandates entrusted to them – or the reimbursement of travel expenses and expenses incurred in the interest of the company – must be the subject of a special report by the auditor to the general meeting.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

A shareholder is a natural or legal person who makes a contribution (in kind, cash or industry) to the company. In return, the company delivers shares (Articles 7 and 51 of the AUSCGIE).

The status of shareholder is regulated by Articles 7 to 9 of the AUSCGIE. Those persons who cannot be shareholders are:

- any natural or legal person who is subject to a prohibition, incapacity or incompatibility provided for by a legal or regulatory provision; and
- minors and incapable adults in companies where they would be liable for the company's debts beyond their contributions.

Company shares are called “*actions*” (in French) in joint stock companies and “*parts sociales*” in other companies (Articles 7 and 51 of the AUSCGIE).

The contribution made by the shareholders determines their rights and obligations within the company:

- a right on the profits made by the company;

- a right on the net assets of the company at the time of their distribution, at the time of dissolution, or at the time of a reduction of the company's capital and intervention in the social affairs of the company;
- an obligation to contribute to the losses in certain forms of company; and
- the right to participate in the vote of shareholders' collective decisions.

The rights and obligations of the shareholders are proportional to their contribution.

In addition, according to Article 54 of the AUSCGIE, clauses that attribute to a shareholder all of the profit made by the company or exempt them from all of the losses – as well as clauses that exclude a shareholder entirely from the profit or make them responsible for all of the losses – are deemed unwritten.

Disagreement between shareholders constitutes a cause for dissolution of commercial companies within the meaning of Article 200 of the AUSCGIE.

In limited liability companies, the shareholders are only liable for the company's debts up to the amount of their contributions. The limited liability companies are:

- the SARL;
- the SAS; and
- the SA.

In the case of debts in such a company, the liability of the shareholder is limited to the loss of the total amount of their contributions in share capital and their contributions in the shareholders' current account.

Shareholders who hold management positions within the company may also be liable – individually or jointly – to the company or third parties, either for breaches of the law or the articles of association (civil or criminal liability) or for faults committed in their management.

5.2 Role of Shareholders in Company Management

The shareholders have a certain right of control over the management of the company, which differs according to the type of company.

SARL Shareholders

Any non-managing shareholder can, twice a year, ask the manager questions in writing about any fact that could jeopardise the continuity of the business. The manager must then provide answers within 15 days, in writing, to the questions asked by the shareholder. Within the same time limit, they must send a copy of the questions and their answers to the auditor, if there is one (Article 157 of the AUSCGIE).

SA and SAS Shareholders

Any shareholder who does not have managerial status may, twice a year, ask questions in writing of the chairperson of the board of directors, the CEO or the managing director (as the case may be) on any fact likely to jeopardise the continuity of the business. The chairperson of the board of directors or the CEO (as the case may be) must then reply, in writing, within 15 days, to the questions asked by the shareholder. Within the same period, they must send a copy of the questions and their answers to the auditor (Article 158 of the AUSCGIE).

The shareholder is also able to direct the actions of the corporate officers, thanks to:

- the holding of ordinary general meetings, during which the corporate documents are controlled and approved (summary financial statements, management reports, inventories, draft resolutions, the auditor's report, and the auditor's special report on regulated agreements (if any);
 - individual action (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**); and
 - corporate action (see **4.8 Consequences and Enforcement of Breach of Directors' Duties**).
- to approve the summary financial statements, the management report and the inventory (Article 140 of the AUSCGIE for the SA, SARL and SAS) – to this end, the aforementioned documents are communicated at least 15 days before the meeting by the company directors;
 - to decide on the allocation of the result (Article 142 of the AUSCGIE); and
 - to determine the allocations to optional reserves, the share of profits to be distributed, and the amount of any retained earnings (Article 144 of the AUSCGIE).

5.3 Shareholder Meetings

All shareholders have the right to participate in the voting of collective decisions (Article 125 of the AUSCGIE). There are two kinds of collective decisions: ordinary decisions and extraordinary decisions (Article 132 of the AUSCGIE). These decisions can be taken within the framework of general meetings or by written consultation (Article 133 of the AUSCGIE). All the deliberations of the shareholders are noted by a minute (Article 134 of the AUSCGIE).

The manager is in charge of convening the general meeting. In the event of their failure to do so, the auditor may substitute for the manager. Failing this, the shareholders may request the convening of the meeting in court.

The methods of convening the meeting are set out in the articles of association. The ordinary general meeting congregates at least once a year (within six months of the end of the financial year). An extension of the deadline may be requested from the president of the competent court ruling on a petition. The purpose of the ordinary general meeting is:

In an SARL and an SA, the decisions are made by a majority of the votes present and represented.

The extraordinary general meeting takes extraordinary collective decisions (ie, decisions to amend the articles of association). It decides by a majority of three quarters of the capital in a SARL and two thirds in an SA.

However, unanimity is required in the case of:

- an increase of the shareholders' commitments;
- transformation into an SAS; and
- transfer of the registered office to a state other than a state party to the AUSCGIE.

In the event of a loss of half of the share capital, an extraordinary general meeting must be convened within four months of the general meeting that recorded this loss, on pain of penal sanctions or request by any interested party for dissolution of the company.

In an SAS, the rules of majority and quorum are set by the articles of association.

5.4 Shareholder Claims

The bases of claim that exist for shareholders against the company or directors are as follows:

- against the company – the shareholders do not have a liability claim against the company; and
- against the directors – see 5.2 Role of Shareholders in Company Management (social action, individual action, alert procedure).

5.5 Disclosure by Shareholders in Publicly Traded Companies

As far as is known, there are no disclosure or other obligations on shareholders in publicly traded companies. There are disclosure obligations regarding beneficial owners of companies generally (see 2.1 Hot Topics in Corporate Governance).

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Pursuant to Article 137 of the AUSCGIE, at the close of each fiscal year, the manager or the board of directors or the managing director (as the case may be) must prepare and close the financial statements in accordance with the provisions of the Uniform Act on the Organisation and Harmonisation of Companies' Accounting.

As required by the revised Article 140 of the AUSCGIE, for an SA, an SAS and – where applicable – a SARL, the annual summary financial statements and the management report are sent to the auditors at least 45 days before the date of the ordinary general meeting. These documents are presented to the general meeting of the company approving the financial statements, which

must be held within six months of the end of the financial year.

6.2 Disclosure of Corporate Governance Arrangements

Pursuant to Article 138 of the AUSCGIE, the manager, the board of directors or the managing director (as the case may be) draws up a management report in which they describe the situation of the company during the past financial year, its foreseeable evolution, the important events that occurred between the closing date of the financial year and the date on which it is drawn up, and – in particular – the prospects for the continuation of the activity, the evolution of the cash-flow situation and the financing plan.

This report is therefore financial, but the AUSCGIE allows for the creation of committees – composed of directors, within the board and under the direction of a director – to deal with particular aspects of the life of the company (Article 437 of the AUSCGIE). Thus, according to Article 437 Section 2 “[The board of directors] may decide to create committees composed of directors to study the questions that it or its chair[person] submits to them for advice. It shall determine the composition and powers of the committees, which shall carry out their activities under its responsibility.”

The AUSCGIE also provides for the mandatory presence of audit committees in companies issuing stock to the public, in order to ensure better corporate governance. The audit committee must report regularly to the board of directors on the performance of its duties and must inform the board of directors without delay of any difficulties encountered (Article 829-1 of the AUSCGIE).

In addition, agreements entered into directly or through an intermediary between the company and one of its managers, directors or shareholders are the subject of a special report by the auditor at the general meeting.

6.3 Companies Registry Filings

Commercial companies are required to make filings with the companies registry of the registered office for the following:

- the appointment or termination of the functions of company executives (Article 124 of the AUSCGIE);
- a draft merger or demerger (filed in the Trade and Personal Property Credit Register of the registered office of the companies concerned at least one month before the date of the first general meeting called to decide on the operation) (Article 194 of the AUSCGIE);
- the dissolution of the company, by filing in the Trade and Personal Property Credit Register the deeds or minutes deciding upon or recording the dissolution and by amending the entry in the Trade and Personal Property Credit Register (Article 202 of the AUSCGIE);
- liquidation of the company by the deposit of the final accounts drawn up by the liquidator, with either the decision of the meeting of shareholders ruling on these liquidation accounts, the discharge of the liquidator's management and the discharge of their mandate, or – failing this – the court decision referred to in the preceding article in order to obtain the striking-off of the company from the Trade and Personal Property Credit Register (Articles 219 and 220 of the AUSCGIE);
- approval of the company's accounts by filing the summary financial statements (ie, the balance sheet, the profit-and-loss account, the financial table of resources and uses, and the annexed statement of the past financial

year) within one month of their approval by the competent body (Article 269 of the AUSCGIE);

- transferable securities (for their enforceability against third parties); and
- transfer of shares (for the enforcement of their rights against third parties) (Articles 319 and 763-1 of the AUSCGIE).

The filings relating to the incorporation or the modification of the company (merger, liquidation of a company) as well as the pledges or the collective procedure are publicly available upon request to the companies registry. However, specific documents such as financial statements are not available. Failure to make these filings entails the unenforceability of the modifications/actions carried out.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

In the SA, the appointment of an auditor is mandatory. It takes place during the constitutive general meeting (for the first appointment). An SA making a public appeal for savings is required to appoint at least two auditors and two deputies. An SA that does not make a public offering is required to appoint one auditor and one substitute.

As regards the other corporate forms, this appointment is optional, except where the company exceeds certain thresholds (see **1.1 Forms of Corporate/Business Organisations**).

The auditor's duties include:

- evaluating the contributions in kind realised at the time of the constitution of a SARL or an SA;

- drafting the summary financial statements;
- presenting the agreements between the company and its shareholders or its directors to the general meeting or the board of directors; and
- making requests to the company's directors concerning all facts likely to compromise the continuity of the operation, which they have noted during the examination of the documents that are communicated to them, or of which they have knowledge in the exercise of their duties.

The auditor is responsible, with respect to the company and third parties, for the harmful consequences of the faults and negligence they may commit in the performance of their duties (insufficient investigation or certification of an inaccurate balance sheet, for example

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Management Report (Article 138 of the AUSCGIE)

The manager, the board of directors, or the managing director (as the case may be) is required to prepare a management report in which they describe the situation of the company during the past financial year, as well as its future situation. This management report is submitted for the approval of the shareholders at the annual general meeting.

Agreements Between the Company's Directors and the Company

In an SA with a board of directors (Article 438 of the AUSCGIE) and an SA with a managing director (Article 502 of the AUSCGIE), the regulated agreements are subject to the authorisation of the members of the board of directors and to the approval of the general meeting ruling on the summary financial statements. For a SARL (Article 350 of the AUSCGIE) and an SAS (Article 853-14 of the AUSCGIE), these agreements are subject to approval by the general meeting.

Prohibited Agreements

The managers of a SARL (Article 356 of the AUSCGIE) and the directors of an SA (Article 450 of the AUSCGIE) are prohibited from contracting loans from the company in any form whatsoever, from being granted an overdraft on a current account or otherwise, as well as from being guaranteed or endorsed by the company in respect of their commitments to third parties. These acts are null and void.

Trends and Developments

Contributed by:

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Houda Law Firm

Houda Law Firm was founded in 1977 in Dakar, Senegal, and consists of a 70-person staff – half of whom are specialised and highly qualified lawyers and legal advisers working to assist clients (such as private companies, public entities and individuals) with all their legal needs in Senegal and the West African Economic and Monetary Union (WAEMU) member states. The

firm opened a branch in Abidjan, Côte d'Ivoire, in 2018, which made it the first foreign law firm from the WAEMU region to be established in the country. The team works on matters related to company incorporation, investment, employment law, taxation, business litigation, and arbitration. Houda Law Firm was certified in September 2020 (ISO 9000-2015).

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Khaled Abou El Houda of Houda Law Firm holds master's degrees in business law and in banking and finance. Registered with the Senegalese Bar since 1999 and authorised to practise

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Chadi Safieddine joined Houda Law Firm in December 2021, where he works as corporate senior legal counsel. Chadi previously worked in a law firm specialised in business law and

in an accounting firm where he managed the legal department. Within Houda Law Firm, he has accumulated experience in the field of corporate law and has been successfully involved in company audits, increasing share capital, mergers, demergers and partial contribution of assets, the sale of companies (up to closing), and the dissolution/liquidation of companies. He has also been in charge of drafting legal opinions and legal consultations in the context of legal advisory missions and assists the team in litigation procedures.



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Corporate Governance and Corporate Social Responsibility in Senegal

Corporate governance and corporate social responsibility (CSR) are two essential elements of modern business practices. Although they may appear to be distinct concepts, they are closely linked.

Corporate governance is the framework that governs how a company is managed and controlled, ensuring that the interests of shareholders and other stakeholders are protected. It involves a clear division of rights and responsibilities between the board of directors, management, and shareholders. Effective corporate governance promotes transparency, accountability and integrity within an organisation.

Developed on the initiative of a number of international institutions (the United Nations, the International Labour Organization, and the OECD), CSR encourages companies to voluntarily integrate sustainable development into their economic policies by systematically taking into account the social, environmental and societal impacts of their activities and thus adopting practices that combine economic logic, social responsibility, and eco-responsibility.

As such, the link between corporate governance and CSR is one of interdependence, with each reinforcing and supporting the other. By way of example, effective corporate governance ensures that the interests of the various stakeholders (including shareholders, employees and customers) are aligned with the long-term objectives of the company. When corporate governance is well established, it provides a framework for integrating CSR principles into strategic decision-making, leading to actions that take both financial and non-financial aspects into account.

Corporate governance also promotes transparency and accountability in decision-making processes. This transparency extends to CSR initiatives, where companies are required to disclose their environmental and social impacts, objectives and progress. Transparency in decision-making enhances the credibility of CSR efforts and builds trust among stakeholders.

Another example is that corporate governance holds directors, managers and employees accountable for their actions. Ethical behaviour is a fundamental element of corporate governance and CSR. By integrating ethical practices into their governance frameworks, companies

establish a culture of responsibility and integrity, thereby strengthening the ethical aspects of CSR.

Finally, in general, corporate governance and CSR both emphasise long-term value creation rather than short-term gains. Integrating CSR into corporate governance practices ensures that sustainability and social impact considerations are taken into account in strategic planning. This approach helps companies manage risk, adapt to market changes, and strengthen their resilience for the future.

CSR therefore brings many benefits to companies and society as a whole:

- improved risk management – companies can more easily identify and manage risks related to ESG factors;
- improved organisational performance – by taking into account the interests of all stakeholders, companies that integrate CSR generally see an improvement in their organisational performance, including greater employee engagement;
- attracting investors and capital – foreign investors in particular are increasingly taking ESG factors into account when making investment decisions; and
- generating a positive social impact – by supporting local communities and promoting ethical business practices, organisations can contribute to sustainable development and the well-being of society as a whole.

In the Senegalese legal context, the concept of CSR is insufficiently taken into account in corporate governance. Indeed, as a reminder, under local law, corporate governance is governed by the Uniform Act on Commercial Companies and Economic Interest Groups (*Acte Uniforme révisé*

relatif au droit des Sociétés Commerciales et du Groupement d'Intérêt Économique, or AUSCGIE). However, this act makes no reference to CSR – only to mandatory rules governing, for example, the composition of the board of directors and shareholders' voting rights.

Apart from the AUSCGIE, an explicit and recent reference to CSR is made in relation to public procurement. Article 4-44 of Decree No 2022-2295 of 28 December 2022 on the Public Procurement Code provides that CSR refers to all actions taken by a company to comply with existing regulations – in particular, its ethical, social and environmental obligations towards its staff and other participating companies, taking into account the impact of its activities on its environment.

In addition, in certain key economic sectors such as mining, certain agreements require companies to invest in the development of local communities hosting their projects. At the regional level, the Economic Community of West African States (ECOWAS) – through Article 11 (2) of Directive C/DIR/3/05/09 of 27 May 2009 on the harmonisation of guidelines and policies in the mining sector – stated that ECOWAS member states must “*ensure that CSR in mining and alternative livelihood programmes subject to this article are part of the conditions for granting a mining right or title*”.

An observation could therefore be made at the local level: for many stakeholders, CSR appears to be more of a constraint. However, as mentioned earlier, CSR can bring many benefits – among which are the following.

- From a social perspective, an appropriate policy implemented for the benefit of a company's employees will help improve their

working conditions, make them aware of the efforts the company is making on their behalf, and – of course – increase their commitment to the company.

- an environmental level, a good waste management policy (and therefore recycling) will enable certain industries to save energy by using this waste as fuel.
- On the economic front, strengthening the capacities of a company's suppliers will enable them to provide better-quality products, which will have an impact on the quality of the products and services provided by the company that has used their services.

It therefore appears that CSR also has a number of advantages for society in terms of good governance. Benefits accrue not only to stakeholders, but also to the companies that adopt this approach – increasing their involvement, contributing to improving their performance and, as a result, creating a competitive advantage over companies that do not practise CSR.

The adaptability of CSR also raises questions. It should be remembered that CSR as a concept was created by Western countries and, because it is still struggling to take root locally, is perceived as a foreign concept. This is reinforced locally by certain CSR policies implemented by large companies' Senegal-based subsidiaries, which are influenced by the policies of their headquarters located thousands of kilometres away and are thus not necessarily connected to the needs of local stakeholders.

All in all, this creates a perception among stakeholders of inadequacy and unsuitability – especially given that, as stated in the introduction, CSR is supposed to be a lever for economic, social and societal development that respects the environment and helps to serve the concerns

of businesses and populations. Consequently, it should be noted that the legislator must emphasise this concept so that economic actors show more interest in social responsibility, in particular. This would involve convincing them of the usefulness of CSR and the need to integrate it into their overall strategy.

In light of the potential benefits of CSR, it therefore seems appropriate that – in the future – executives and managers of Senegalese companies should be trained on the potential of CSR and how they can make the best use of it. It is also important to be pragmatic and to contextualise CSR more by initiating locally designed policies that take into account the real needs of stakeholders and the company's strategy, so that the result is a convergence of interests.

Finally, it seems crucial to optimise the voluntary nature of CSR by legislating and adopting and harmonising incentive policies for companies, as well as implementing sectoral policies for the benefit of these companies, while taking into account the opinions, perceptions and feedback from the grassroots level (ie, the population, civil society and trade unions).

It would be interesting to draw inspiration from jurisdictions where a genuine legal framework has been established for CSR in corporate governance. It is now recognised in the EU (especially in France) that CSR has an impact on all companies, regardless of their size, as they are increasingly required – either because they are encouraged to do so by the law or by the market, civil society or NGOs, or based on their own initiative – to integrate social and environmental concerns into their activities and interactions with other actors and stakeholders.

To achieve its CSR objectives and address new social and environmental challenges, the French legislature has intervened on several occasions to indicate what responsible behaviour should be for large companies. In terms of legal incentives, France has had to transpose the new Directive (EU) 2022/2464 of 14 December 2022 (the “*Corporate Sustainability Reporting Directive*” (CSRD)) into national law. The CSRD determines the scope of sustainability information that certain companies must publish in their management reports (including a sustainability statement), according to a phased timetable.

Ultimately, Senegalese law-makers could draw inspiration from certain foreign laws that are well ahead of the curve on this issue and which define the terms and conditions for implementing CSR.

They could also draw on CSR models to instil certain values and obligations in companies.

Finally, the establishment of a clear legal framework will enable companies and other investors to distinguish CSR from local content requirements (ie, the obligation to allocate a minimum percentage of capital to local Senegalese shareholders) or the obligation for extractive companies to contribute to the Local Community Development Support Fund (*Fonds d’Appui au Développement Local*, or FADL). These requirements and obligations are mandatory and not incentive-based.

SERBIA

Trends and Developments

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Gecić Law

Gecić Law is one of the foremost innovative law firms in South-Eastern Europe. Committed to redefining the role of law firms in this burgeoning regional market, Gecić Law advises international and local clients across a wide range of industries and both public and private sectors, guiding them through the region's complex legal landscape across multiple practice areas. Founded in 2015 by leading independent legal minds and seasoned professionals with a shared vision, the firm's team includes graduates of top-tier universities in the USA

and Europe, each bringing extensive local and international expertise. This diversity of backgrounds enables the firm to deliver innovative, pragmatic solutions to even the most intricate legal challenges. Gecić Law is a proud member of two elite global alliances, extending its capabilities and presence worldwide. The firm has also earned numerous accolades from some of the most respected international legal rankings and professional associations across various practice areas.

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During his studies, Marko participated in numerous legal clinics, workshops, and conferences in various areas of law and completed a specialist course in international law (University of Pittsburgh). Before joining Gecić Law, Marko completed his internship at a reputable regional law firm, where he gained knowledge and experience in commercial and contract law.

Marko received numerous awards for his achievements, including the University of Belgrade award for the best student thesis in the school year 2022/2023. He has also received scholarships from the Faculty of Law and one of the University of Belgrade's endowments.

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Trends and Developments in Corporate Governance in Serbia 2025

Serbia's corporate governance landscape is experiencing significant transformation as the country aligns itself with EU standards and modernises its regulatory framework. In 2024-2025, a series of reforms have been launched to update company legislation, strengthen the governance of state-owned enterprises, incorporate ESG principles, and further liberalise markets. These initiatives coincide with Serbia's deepening integration into European markets, most notably through its accession to the Single Euro Payments Area (SEPA) and preparations for eventual EU membership. As Serbia continues its path toward European integration, its corporate governance framework is evolving to meet international standards while remaining attuned to local market realities, with a growing emphasis on sustainability and transparency.

Evolution of the Corporate Governance Framework in Serbia

One of the most significant developments in Serbian corporate governance is the implementation of the Act on Management of Companies Owned by the Republic of Serbia, adopted by the International Monetary Fund's recommendations. This legislation aims to advance corporatisation, improve management practices, and transform the legal structure of state-owned enterprises. Under the new Act, enterprises owned by the Republic of Serbia must transform into corporations (joint-stock or limited liability companies) by the end of 2025.

The Act establishes a centralised ownership management framework, with the Ministry of Economic Affairs as the primary oversight body. In the energy sector, specific provisions delegate oversight responsibilities to the Ministry of Energy for electricity production and supply.

At the same time, the Republic Commission for Energy Networks supervises electricity transmission and natural gas transportation operations.

Importantly, these overseeing institutions do not directly manage the corporations but rather monitor and enhance corporate governance, with authority to implement emergency measures if operational disruptions occur. This approach aims to improve the efficiency and transparency of state-owned enterprises while maintaining appropriate oversight.

Article 18 of the Act presents various situations in which a business company owned by the Republic of Serbia must obtain government approval, reflecting a balanced approach between operational autonomy and state supervision for entities of strategic importance.

The primary sources of corporate governance legislation in Serbia are:

- the Companies Act;
- the Banks Act;
- the Auditing Act; and
- the Capital Market Act.

This regulatory framework has been continuously enhanced since the post-socialist transition period, with significant corporate and security legislation interventions to establish market-based economic principles and improve corporate governance practices.

Serbia has taken decisive steps to modernise its company laws per EU legislation. The Companies Act has been amended to incorporate European corporate forms and practices. Serbia's law now recognises the *Societas Europaea* (SE), a European public company, and European Economic Interest Groupings (EEIGs) as permis-

sible business entities. These EU-harmonized forms are slated to become available in Serbia by 2027, reflecting the government's commitment to integrating with the European corporate framework. Allowing SEs and EEIGs means that Serbian businesses will eventually be able to use the same cross-border corporate vehicles as those in EU member states, facilitating regional investments and partnerships. While these provisions are in place in the legislation, their implementation is timed with Serbia's anticipated EU accession timeline.

In addition to new business forms, Serbia is aligning its laws with recent EU directives. Pending legislation on cross-border mergers, conversions, and divisions will transpose EU rules that make it easier for companies to restructure across borders. Another area of upcoming alignment is board diversity: the EU's 2022 Directive on gender balance (requiring a minimum representation of women on corporate boards) will necessitate changes in Serbian company law. Though not yet in force, Serbia is expected to introduce gender diversity obligations for listed company boards soon as part of its EU harmonisation efforts.

Digitalisation

The digitalisation of corporate processes has also advanced. As of May 2023, electronic filing of company incorporation became mandatory for all business entities. The Serbian Business Registers Agency (APR) now operates as a one-stop electronic system for company registration and information access. Company data is stored in a digital database, which is being made technically ready to interconnect with the EU's Business Registers Interconnection System (BRIS) once Serbia joins the EU. These measures streamline business start-up procedures domestically and ensure that Serbia's corporate

registry can seamlessly integrate with European networks. Ongoing work to align with the EU's Digital Tools Directive (2019/1151) is expected to further enable online shareholder meetings and cross-border online registration, eliminating remaining paper-based formalities.

The Serbian Corporate Governance Act

Serbia's legal framework for corporate governance is already aligned mainly with EU principles. The Serbian Corporate Governance Act is based on OECD and EU best practices, guiding board responsibilities, shareholder rights, and transparency for listed companies. However, legislative modernisation continues in areas such as takeover regulation: a new Takeover Law is under consideration to fully implement the EU Takeover Directive and ensure equitable treatment of minority shareholders in acquisitions. The trend converges with EU standards: Serbia is updating its company law regime to make it more modern, transparent, and compatible with Europe's internal market. This creates a more predictable environment for both domestic and foreign investors, signalling that Serbia's corporate legislation is keeping pace with international norms.

Recent Developments in Corporate Governance

Reform of state-owned enterprises

The reform of state-owned enterprises (SOEs) has become a central pillar of Serbia's governance improvements in 2025. Historically, many large SOEs in Serbia (spanning energy, utilities, infrastructure, and other sectors) suffered from politicised management, inefficiencies, and occasional fiscal drains. Recognising this, the Serbian government introduced a new Management of Public Enterprises Act to overhaul how SOEs are governed and overseen. This reform is being carried out in line with international best

practices and is partly driven by commitments under Serbia's arrangement with the International Monetary Fund (IMF).

Under the new framework, SOE governance is being professionalised and depoliticised. Directors and board members of state-owned companies will be classified as public officials, subject them to stricter anti-corruption rules and transparency obligations. Article 18 of the Act presents various situations in which a business company owned by the Republic of Serbia must obtain government approval, reflecting a balanced approach between operational autonomy and state supervision for entities of strategic importance.

This change reverses a 2021 interpretation that had weakened oversight and reestablishes accountability for those managing public assets. The revised provisions state that any acting director can only serve for a limited period, with a maximum cumulative duration. A qualified permanent director must also be appointed through a transparent public competition within a specified deadline. Serbia aims to ensure merit-based appointments and stable leadership in its state enterprises by closing this loophole.

Additionally, the new Act strengthens boards of directors and introduces clearer responsibilities for SOE supervisory bodies. It includes measures to prevent the misuse of public resources, especially around election cycles. Enhanced reporting requirements and performance monitoring are being implemented, aligning with OECD Guidelines on Corporate Governance of State-Owned Enterprises.

These legislative changes are expected to improve Serbia's task ahead of time to enforce the new rules fully:

- appoint truly independent, qualified directors;
- publish transparent financial results; and
- subject SOEs to market discipline.

Continued monitoring by international partners (EU, IMF, World Bank) is likely, given the importance of SOE reform for Serbia's fiscal health and EU accession prospects. Serbia's state-owned enterprises are finally being brought under a modern governance regime. This should lead to more efficient public companies and a level playing field where private and public businesses compete fairly, boosting overall economic performance.

Amendments to the Company Act

In early 2025, the Serbian government adopted a Draft Act on Amendments to the Company Act that introduces more precise definitions and rules for cross-border corporate transformations, aligning with EU standards. The legislation defines:

- detailed procedures covering the drafting and publication of contracts;
- reports from competent authorities and auditors;
- registration requirements;
- the legal consequences of these transactions;
- the formation process;
- management structure;
- share capital requirements; and
- procedures for converting a joint-stock company into a European company; or
- transferring its registered seat to other EU member states.

The amendments introduce a harmonised framework for cross-border mergers with EU entities, eliminating the need for liquidation procedures. This reform aligns with Directive (EU) 2019/2121 on cross-border conversions and mergers. The

finalised procedures require companies to prepare a joint draft merger agreement, publish it at least one month before adoption, and obtain independent auditor assessments of asset valuations. Notably, the Act mandates a notarial deed to confirm compliance, with registration effects binding only after both Serbian and foreign authorities validate the merger.

Introducing the European public limited-liability company (SE) enables Serbian firms to operate under a pan-European legal structure. An SE can be formed via a merger (with at least one Serbian joint-stock company), as a holding company, or through a subsidiary establishment. Key requirements include a minimum share capital of EUR120,000 (converted to dinars at the median exchange rate) and dual registration in Serbian and EU business registers. This structure allows Serbian SEs to transfer their registered office to EU states without dissolution, facilitating seamless market entry. However, governance adjustments are necessary: SEs must adopt either a one-tier (board of directors) or two-tier (management and supervisory board) system, diverging from Serbia's traditional model.

The amendments authorise European Economic Interest Groupings (EEIGs), enabling Serbian and EU businesses to form joint R&D, production, or distribution alliances. Unlike traditional joint ventures, EEIGs lack legal personality, meaning members bear unlimited joint liability for obligations. This structure is ideal for SMEs collaborating on EU-funded projects, as it allows profit-sharing without creating a new corporate entity.

These amendments will take effect on 1 January 2027. The National Assembly is advised to adopt the Act under an urgent procedure to ensure Serbia's timely preparation for EU integration.

While the amendments advance Serbia's harmonisation with the EU *acquis*, gaps persist. The 2024 EU Progress Report notes Serbia's incomplete transposition of directives on digital tools in company law and takeover bids, areas not fully addressed by the current reforms.

Alignment with EU Acquis

Serbia's path to full EU alignment

Serbia is actively working toward achieving complete alignment with the EU *acquis* and practice by the end of 2026, with corporate governance being a crucial area of this harmonisation process. The abovementioned amendments to the Company Act stem directly from Serbia's obligations in the EU accession process, specifically under Chapter 6 (Company Act) of the Stabilization and Association Agreement between Serbia and the EU.

Introducing European corporate forms and cross-border mechanisms represents a significant step in this alignment process. By establishing *Societas Europaea* and European Economic Interest Groupings, Serbia is launching itself into a more integrated corporate landscape that facilitates business operations across Serbian and EU markets.

Impact on Serbian companies

The ongoing EU alignment process has far-reaching implications for Serbian businesses. Companies must adapt to new corporate governance standards and familiarise themselves with unfamiliar European corporate forms. This adaptation requires investment in legal expertise, corporate restructuring, and governance training.

These changes offer significant opportunities for Serbian businesses with international ambitions. The ability to engage in cross-border mergers

and acquisitions without liquidation procedures streamlines expansion into EU markets. Similarly, establishing European corporate forms provides Serbian companies with familiar structures when operating across the EU, potentially reducing administrative burdens and enhancing their competitiveness in the European market.

However, these benefits come with increased compliance requirements and administrative adjustments. Companies must balance the opportunities for European expansion with the costs of adapting to new governance frameworks and reporting obligations.

ESG Governance and Compliance

The rise of ESG requirements

Environmental, Social, and Governance (ESG) criteria have gained increasing importance in the Serbian business landscape, driven primarily by European regulations and global sustainability trends. The EU's Corporate Sustainability Reporting Directive (CSRD) is transforming the ESG reporting landscape, with 12 sector-agnostic European Sustainability Reporting Standards (ESRSs) requiring disclosures on hundreds of metrics and targets.

Although Serbia is not yet a member of the European Union, EU requirements significantly affect Serbian businesses – especially those involved in European supply chains or trying to access EU markets and financing. The concept of “*Due Diligence*” has become particularly important for Serbian companies, especially small and medium-sized enterprises, that want to become suppliers to major European corporations.

Non-financial reporting framework

Serbia has implemented non-financial reporting requirements through its Accounting Act, which obliges companies with over 500 employees to

publish non-financial reports. In 2021, Smart Kolektiv and the Responsible Business Forum Serbia published a handbook titled “*Step by Step to the Non-Financial Report*” to guide companies through this process, providing insights into the context, requirements, and best practices for non-financial reporting.

The handbook addresses the challenges companies face when navigating various reporting requirements and methodologies. It aims to support both legal compliance with the Accounting Act and broader business sustainability efforts. This resource has been particularly valuable as Serbian companies adjust to more comprehensive ESG reporting standards.

ESG criteria and their impact on Serbian businesses

Since 2024, ESG regulations have mandated that Serbian companies seeking access to the European market and opportunities as suppliers for major corporations must embrace comprehensive sustainability analysis. These regulations delineate over 20 specific criteria addressing human rights violations, environmental impacts, child and forced labour, workplace safety, freedom of workers' associations, and the right to a healthy natural environment.

Failure to comply with these rigorous ESG requirements can lead to substantial setbacks for Serbian businesses, including:

- diminished competitiveness;
- tarnished reputation;
- reduced added value; and
- increased energy and resource consumption.

The directive defines more than 20 human rights requirements and more than 10 environmental impact criteria that companies must address.

European companies are now obliged to analyse their partners' social and environmental impacts on global supply chains, directly affecting domestic suppliers in Serbia. Similarly, foreign banks are expected to conduct ESG analyses when deciding on loans and guarantees, making ESG compliance increasingly crucial for access to capital.

To support Serbian businesses in this transition, the United Nations Development Program, in collaboration with the Serbian Development Agency and Smart Collective, has established initiatives like the “*ESG Practitioner*” training program. These initiatives aim to empower businesses to adopt and implement sustainable and ethical practices, demonstrating the growing institutional support for ESG implementation in Serbia.

Legal framework for ESG issues

While Serbia has legal regulations covering environment, labour relations, occupational safety, human rights, data protection, and corporate governance, the extensive European ESG legislation has not yet been fully transposed. State policies and strategies determining how domestic companies will align their operations with ESG requirements are still developing, particularly for companies directly obligated or affected by value chains.

Companies that are part of international groups have an advantage in this respect, as they can transfer policies and strategies from the group level and implement them more quickly locally. The journey toward comprehensive ESG integration remains more challenging for independent Serbian businesses, highlighting the need for additional guidance and support from regulatory bodies and industry associations.

Practical Implications and Future Outlook Convergence with European standards

The analysis of Serbian corporate governance codes reveals a high level of convergence with codes from EU member states. This convergence reflects a recognition that good corporate governance practices benefit listed companies, markets, and all stakeholders. As Serbia continues its EU integration process, we can expect further harmonisation of corporate governance standards and practices.

The evolving market for corporate control

The market for corporate control in Serbia has matured significantly since the early transition period, serving as an essential external corporate governance mechanism. The continued development of this market enhances discipline among corporate managers and contributes to more efficient resource allocation within the economy.

Increased focus on small and medium enterprises

Corporate governance has traditionally been associated with large public companies, albeit recent developments indicate growing attention to governance practices in small and medium-sized enterprises. The Chamber of Commerce and Industry of Serbia's corporate governance code specifically targets these companies, recognising their significant economic contribution.

For SMEs, improved corporate governance can streamline business processes, establish a clearer division of responsibilities, enhance accountability, and ultimately lead to better performance and competitiveness. This focus on SMEs is significant given their role in Serbia's economic development and potential integration into European value chains.

Challenges for SMEs and digital transformation

Despite the reforms mentioned earlier, Serbia continues to struggle to implement strong corporate governance practices throughout its economy. SMEs, vital to Serbia's economic structure, often fall short in governance standards and digital technology adoption. Addressing these shortcomings is crucial for achieving inclusive and sustainable growth.

As these companies grow or seek outside investment, the lack of a governance structure can become a hurdle. For instance, accessing bank financing or venture capital is harder without transparent financial reporting and sound management practices.

Another ongoing challenge is the digitalisation gap. Serbia has made good progress in e-government and digital infrastructure for businesses, yet there are still notable gaps in implementation and usage. A 2024 World Bank-supported report on Serbia's business environment highlighted that despite reforms, SMEs continue to face high parafiscal fees and cumbersome procedures, partly due to limited integration of digital services.

Moreover, digitalisation within companies is uneven. Larger Serbian companies have generally adopted modern IT systems for finance, inventory, and customer management. However, many smaller businesses operate with minimal digital tools. Cybersecurity and data protection present additional challenges in the digital realm.

In summary, the challenges of SME governance and digital gaps are recognised hurdles in Serbia's overall progress. Tackling them will require a combination of policy support, education, and market pressure. As EU integration

looms, Serbian SMEs must increasingly meet higher compliance and technological standards to compete. Closing these gaps is not just a bureaucratic exercise; it is about ensuring that the positive reforms at the top, in regulations and large companies, permeate the entire economy. Only then will the benefits of corporate governance improvements and market integration be fully realised for Serbian society.

Bridging governance gaps

Despite substantial progress, gaps remain in Serbia's corporate governance framework, particularly regarding the application of ESG principles and the integration of sustainability into corporate strategy. Companies are increasingly expected to address these gaps to comply with regulations and meet the expectations of investors, partners, and customers.

Conclusion: Towards European Integration

Corporate governance in Serbia has evolved significantly, moving from basic frameworks toward sophisticated systems that incorporate international best practices and address emerging sustainability concerns. Serbia's ongoing alignment with the EU *acquis*, particularly in areas like cross-border mergers and European corporate forms, demonstrates its commitment to integration with European markets.

The introduction of ESG requirements presents both challenges and opportunities for Serbian businesses. While compliance demands resources and expertise, it also encourages more sustainable and responsible business practices that can enhance long-term value creation and competitiveness.

As Serbia continues its European integration journey, we can expect corporate governance to remain dynamic, with continued legislative

developments, increased emphasis on transparency and accountability, and greater integration of sustainability principles. Companies proactively adapting to these changes will be better positioned to thrive in this evolving landscape, attracting investment, building stakeholder trust, and contributing to Serbia's economic development.

Overall, the trajectory for corporate governance in Serbia is a gradual but meaningful improvement. Continuous legislative reform, driven partly by the EU accession process, creates a more robust legal backbone for governance. Equally important, however, will be the evolution of corporate culture. As Serbian companies compete for capital and partnerships internationally, they

are coming to appreciate that sound corporate governance is a competitive advantage. Directors and executives are increasingly expected to balance entrepreneurial agility with adherence to governance principles of transparency, fairness, and responsibility. In the years to come, Serbia's ability to uphold these principles – in both the private and public sectors – will play a pivotal role in sustaining investor trust and supporting the country's economic ambitions. The intersection of traditional governance concerns with newer ESG considerations creates a rich area for legal innovation and expertise, ensuring corporate governance remains a central consideration for businesses operating in Serbia in 2025 and beyond.

SOUTH AFRICA



Law and Practice

Contributed by:

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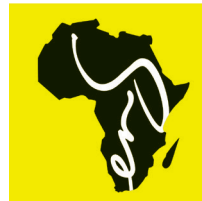
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ENS africa

1. Introductory

1.1 Forms of Corporate/Business Organisations

A company incorporated in terms of the Companies Act, No 71 of 2008, as amended (the “Companies Act”), is the principal form of corporate/business organisation used in South Africa. Companies are separate legal entities with shareholders that provide share capital (equity) and in certain instances debt finance to the company, and have a board of directors that manages the company and its affairs. The Companies Act distinguishes between two broad categories of companies: profit companies and non-profit companies.

Profit Companies

Profit companies include the following entities with their suffixes shown alongside:

- public companies – Limited/Ltd;
- private companies – Proprietary Limited/(Pty) Ltd;
- personal liability companies – Incorporated/ Inc.; and
- state-owned companies – SOC Ltd.

A private company cannot offer its securities to the public, and its memorandum of incorporation (MOI) must restrict the transferability of its shares/securities.

A public company can freely transfer its shares to any member of the public. Public companies are ordinarily listed on a stock exchange, with the primary stock exchange in South Africa being the Johannesburg Stock Exchange (JSE).

Personal liability companies are private companies in which former and current directors may be held jointly and severally liable for any

debts and liabilities incurred during their tenure in office. Businesses offering professional services, such as audit and law firms, are examples of such entities.

Non-Profit Companies

In addition to the various types of profit companies discussed above, the Companies Act provides for the incorporation of non-profit companies, which may be incorporated with or without members. Names of non-profit companies end with the expression “NPC”. Non-profit companies are also limited liability corporations and are exempt from various provisions of the Companies Act.

Ring-Fenced Companies

When a company is ring-fenced (indicated by “(RF)” in its title), third parties are regarded as having notice and knowledge of any restrictive conditions contained in its MOI.

Other Business Entity Models

Further business entity models used in South Africa include:

- partnerships, which are not separate legal entities distinct from persons comprising the partnership;
- trusts, which have a separate legal personality for certain purposes, usually provided in the deed of trust, such as taxation and perpetual succession;
- sole proprietorships, in which a sole proprietor trades under their own name with no limited liability – ie, there is no separation between their personal assets and liabilities and those of the business; and
- close corporations, which are corporations that do not exceed a limited number of members and are simplified limited liability corporations (it should be noted that the ability to

form new close corporations ceased as of 1 May 2011).

Foreign Companies

Foreign companies that carry on business activities within South Africa may be required to register as an external company in South Africa and are only required to comply with certain provisions of the Companies Act.

1.2 Sources of Corporate Governance Requirements

For this chapter and unless otherwise specified, the term “*corporate governance*” is used widely to include the laws listed below as well as practices and rules (effectively guidelines) that are imposed through instruments such as the stock exchange rules and the King Report on Corporate Governance for South Africa (“*King IV*”).

The principal sources of corporate governance in South Africa are as follows.

- The Companies Act, which replaced the 1973 Companies Act with effect from 1 May 2011, and which (with certain surviving provisions from the 1973 Companies Act applicable to the winding-up and liquidation of companies) is the regime that governs the incorporation and management of companies in South Africa and which has been amended in terms of the Companies Amendment Act No 16 of 2024 (Companies Amendment Act) and the Companies Second Amendment Act No 17 of 2024 (Companies Second Amendment Act), which were both signed into law on 26 July 2024 and are discussed in further detail in **2.1 Hot Topics in Corporate Governance**.
- The common law and the Companies Act with respect to the regulation of the fiduciary duties of directors of companies.
- The Companies Regulations, 2011 (the “*Regulations*”), which came into effect with the Companies Act on 1 May 2011 and have subsequently been amended by the Companies Amendment Regulations 2023.
- The JSE Listings Requirements (the “*Listings Requirements*”), which apply to public companies listed on the JSE (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**).
- The Financial Markets Act, No 19 of 2012, which, amongst other things, regulates financial markets and exchanges, and contains the South African Insider Trading and Market Abuse Legislation.
- King IV, issued by the Institute of Directors in Southern Africa. The latest iteration of the code came into effect on 1 April 2017 (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** for further details). It is worth noting that a draft King V Code has been published for public comment (see **2.1 Hot Topics in Corporate Governance** for further details).
- The common law (derived from case law).
- Sector-specific legislation and/or codes that regulate the corporate governance of entities within the same industry – for example, the Code for Responsible Investing in South Africa prescribes governance standards for institutional investors as asset owners (pension funds and insurance companies, etc) and their service providers (asset managers, fund managers, etc).
- The Public Finance Management Act, No 1 of 1999, contains financial governance measures and the responsibilities of persons entrusted with financial management of state-owned entities.

The key source of a company’s corporate governance requirements is its constitutional docu-

ment (eg, MOI, articles of association or trust deeds). The Companies Act contains both mandatory “unalterable” provisions and default “alterable” provisions, in terms of which the latter allows for variation by a company in its MOI. Significantly, certain provisions relating to corporate governance concerns (such as shareholder rights, annual disclosure requirements in the case of regulated companies and directors’ duties) cannot be altered by the MOI.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

In addition to the requirements of the sources referred to in 1.2 Sources of Corporate Governance Requirements, companies with shares that are publicly traded and listed on the JSE are required to comply with the following.

The Listings Requirements

The Listings Requirements impose continuing obligations on issuers, including standards of disclosure and specific corporate governance practices relating to:

- the board composition of a company;
- the appointment of various board committees, such as the remuneration committee, as well as statutory committees such as the audit and social and ethics committees; and
- the adoption of particular governance-related policies and compliance with King IV.

King IV

King IV is South Africa’s authoritative corporate governance code. While King IV compliance is voluntary, the Listings Requirements oblige issuers to adopt certain of its recommendations, with the remainder being implemented in accordance with King IV’s “*apply and explain*”

disclosure policy. In order to give effect to this policy, a company should:

- apply the recommended practices meticulously, with common sense, and proportionally in accordance with the company’s size and resources, and the extent and complexity of its activities; and
- provide a narrative explanation of that application with reference to the recommended practices.

It is important to note that non-compliance with the principles of King IV can be interpreted as non-compliance with the Listings Requirements and result in censures, penalties and/or enforcement action being imposed by the JSE.

In addition to the annual reporting requirement, certain facets of governance as set out in King IV must be complied with in terms of the Listings Requirements.

Whilst King IV is intended to apply to companies, it is also intended to apply to other organisations irrespective of their form of incorporation, to broaden acceptance of corporate governance by making it accessible and relevant so that it can be applied across various sectors, organisations and organs of state.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance Greylisting of South Africa

In late February 2023, South Africa was “grey-listed” by the Financial Action Task Force (FATF) for failing to comply with certain international standards relating to the combatting of money laundering and other serious financial crimes. In response to the 2021 FATF Mutual Evalua-

tion Report, which placed the country on the list of states that failed to meet these standards, the General Law (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act, No 22 of 2022 (GLAA) was signed into law in December 2022. The GLAA amends various pieces of legislation, including the Companies Act and the Trust Property Control Act, No 57 of 1988 (TPCA), which has an impact on corporate governance.

For instance, the GLAA has broadened the legislation set out in Section 69 (8)(b)(iv) of the Companies Act, which would disqualify a person from being a director, to include the Protection of Constitutional Democracy Against Terrorist and Related Activities Act, No 33 of 2004 and the Tax Administration Act, No 28 of 2011, in addition to the Companies Act; the Insolvency Act, No 24 of 1936; the Close Corporations Act, No 69 of 1984; the Competition Act, No 89 of 1998; the Financial Intelligence Centre Act, No 38 of 2001 (FICA); the Financial Markets Act, No 19 of 2012; and Chapter 2 of the Prevention and Combating of Corrupt Activities Act, No 12 of 2004 if such person is convicted of an offence thereunder. Furthermore, if such person is subject to a resolution adopted by the Security Council of the United Nations providing for financial sanctions, they would be disqualified from being a director of a company.

The GLAA also introduced the concept of “*beneficial owner*” to the Companies Act (see **5.5 Disclosure by Shareholders in Publicly Traded Companies**). Regarding trusts, the GLAA introduced new offences, in the case of the TPCA, for trustees who fail to comply with the newly introduced provisions relating to the establishment, maintenance and submission of prescribed information relating to beneficial owners of trusts and accountable institutions used by

trustees, and for trustees who fail to make specified disclosures to accountable institutions. A trustee who fails to comply with the above obligations will have committed an offence and on conviction can be liable to a fine not exceeding ZAR10 million, or imprisonment not exceeding five years, or both.

According to a media statement published by the Department of National Treasury on 21 February 2025, South Africa is now deemed to have addressed or largely addressed 20 of the 22 action items in its Action Plan, leaving two items to be addressed in the next reporting period, which runs from March 2025 to June 2025. Once the remaining action items have been addressed, this is likely to enable South Africa to exit the FATF Greylist in October 2025.

It is also worth noting that the National Treasury published the draft General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Bill, 2024 (the GLAA Bill) in December 2024, which aims to demonstrate South Africa’s commitment to strengthening its anti-money laundering and combatting the financing of terrorism system by addressing the deficiencies identified by the FATF in its Mutual Evaluation Report.

In this regard, the GLAA Bill proposes amendments to various pieces of legislation, including the Companies Act, so as to empower the Companies and Intellectual Property Commission (CIPC) to:

- deregister a company that fails to submit a securities register within a certain period; and
- impose administrative penalties.

Furthermore, the GLAA Bill seeks to empower the Companies Tribunal to review a decision of the CIPC to impose an administrative fine.

The deadline to submit public comments on the GLAA Bill was 6 February 2025.

Companies Amendment Act and Companies Second Amendment Act

A significant legal development in corporate governance in South Africa was the introduction of the Companies Amendment Act No 16 of 2024 (Companies Amendment Act) and the Companies Second Amendment Act No 17 of 2024 (Companies Second Amendment Act), which were both signed into law on 26 July 2024. On 27 December 2024, the President proclaimed in Government Gazette No 51837 that certain sections of the Companies Amendment Act and the entirety of the Companies Second Amendment Act came into effect.

The key pillars of the Companies Amendment Act as taken from the Memorandum on the Objects of the Companies Amendment Bill 2023 (ie, Bill B27B-2023, the predecessor to the Companies Amendment Act – the “*Bill*”) include:

- enhancing the ease of doing business; and
- achieving equity between directors and senior management on the one hand, and shareholders and workers on the other hand, as well as addressing public concerns regarding high levels of inequality in society.

It is worth noting that the original version of the Bill published in 2021 contained a third pillar – namely, to counter money laundering and terrorism which, as discussed above, has been addressed by the passing of the GLAA.

The Companies Second Amendment Act is aimed at implementing certain recommendations of the Zondo Commission.

In summary, the Companies Amendment Act and the Companies Second Amendment Act have both introduced amendments to the Companies Act that have an impact on corporate governance in South Africa. These amendments include, inter alia, new requirements relating to social and ethics committees (SECs), greater access to company information and the disclosure of directors’ remuneration.

New Draft of the King Code – King V

The Institute of Directors of South Africa (IoDSA) published a media statement on 24 February 2025 announcing that a draft of the new version of the King Code – ie, the King V Draft – was available for public comment and that the deadline to submit public comments was 4 April 2025.

The objectives of King V are to:

- take local and global developments since King IV was launched in 2016 into consideration, by incorporating critical shifts such as the recent amendments to the Companies Act, evolving practices in remuneration governance, global developments in sustainability reporting, and the rapidly advancing technological landscape;
- simplify King V and make it more user-friendly and accessible; and
- develop a standardised approach to the disclosure of King V’s application to assist organisations with internal monitoring and disclosure of implementation of practices, and to enhance accountability and comparability across different organisations.

2.2 ESG Considerations

The important ESG issues in South Africa include the attainment of sustainable development, a just energy transition, black economic empowerment, climate change resilience, employment equity, improved governance and the introduction of anti-corruption practices. South African regulators and certain organisations have taken various steps to address these issues, some of which are discussed below.

Obligations of JSE-Listed Companies

The majority of ESG disclosures or reporting obligations are voluntary. However, companies listed on the JSE have mandatory reporting obligations with respect to sustainability. In this regard, the Listings Requirements suggest that integrated reporting on sustainability is to be applied on an “*apply and explain basis*”.

King IV requires companies to report annually in an integrated manner and to promote good governance and transparency in leadership and decision-making. King IV also emphasises sustainability reporting. In July 2021, a King IV Guidance document titled “*Responsibilities of Governing Bodies in Responding to Climate Change*” was published in order to assist governing bodies to respond to climate change and to take the required action.

Furthermore, the JSE launched its JSE Sustainability Disclosure Guidance and JSE Climate Change Disclosure Guidance in 2022. The JSE’s disclosure guidance documents are based on international best practice and are an important distillation of the recommendations of multiple global initiatives on sustainability and climate risk disclosure, including GRI Sustainability Reporting Standards, the Taskforce on Climate-related Financial Disclosures recommendations, the IFRS Foundation’s ISSB prototypes and the

Value Reporting Foundation’s Integrated Reporting Framework and Sustainability Accounting Standards Boards. They are also not mandatory, but bring much-needed guidance for consistent, comparable, transparent and reliable disclosures.

Regulation 28 of South Africa’s Pensions Funds Act, No 24 of 1956 requires funds to consider all factors (including ESG) that may be relevant to the long-term success of a fund. In this regard, a guidance note published in 2019 by the Financial Sector Conduct Authority (FSCA) sets out the FSCA’s expectations regarding certain disclosure and reporting requirements relating to sustainability.

South Africa’s first national Green Finance Taxonomy was published in April 2022. Although reporting against the taxonomy is not yet mandatory, it provides a useful benchmark for investors, issuers, lenders and other financial sector participants to track, monitor and demonstrate the credentials of their green activities in a more consistent and efficient way.

ESG reporting requirements are also contained in specific legislation that seeks to deal with environmental impact – eg, reporting obligations stipulated as conditions to environmental authorisations under the National Environmental Management Act, No 107 of 1998 or conditions to atmospheric emission licences under the National Environmental Management: Air Quality Act, No 39 of 2004. Furthermore, certain categories of emitters are required to report on their emissions under the National Greenhouse Gas Emission Reporting Regulations (published in GN 275 of 3 April 2017) (GHG Reporting Regulations). Sectors covered by the GHG Reporting Regulations include energy, transport, industry, agriculture and forestry.

Specific affirmative action and reporting obligations are also imposed on “*designated employers*” subject to the Employment Equity Act, No 55 of 1998, as amended. In the private sector, a designated employer is an employer who employs 50 or more employees, or who has otherwise been declared to be a designated employer in terms of a collective agreement. In addition to prohibiting unfair discrimination in the workplace, the Employment Equity Act requires that designated employers take progressive measures to improve the representation of suitably qualified employees from designated groups (South Africans who are black, women or people with disabilities) in the workplace. The legislative framework seeks to achieve this improved representation of suitably qualified employees from designated groups by requiring designated employers to form and consult with an Employment Equity Committee (made up of trade union and employee representatives), develop and implement an Employment Equity Plan and submit annual Employment Equity Reports to the Department of Employment and Labour.

Notably, the Employment Equity Act has been recently amended. Amongst other things, the recent amendments to the Employment Equity Act and its regulations require designated employers to meet sector-specific employment equity targets (ie, targeted percentages of people from designated groups in the top four occupational levels) over a five-year period. These targets have been determined by the Minister of Employment and Labour. Designated employers who do not meet these sectoral targets after the five-year period will be required to demonstrate to the Department of Employment and Labour that there were justifiable reasons for having not met the sectoral targets. Furthermore, a certificate of compliance with the Employment Equity Act (issued by the Department of Employment

and Labour) is now a prerequisite to conducting any business with the State or any organ of state.

Broad-Based Black Economic Empowerment (B-BBEE) is a policy of the South African government, which is aimed at increasing participation by previously disadvantaged South Africans in economic activities. The Broad-Based Black Economic Empowerment Act 53 of 2003, as amended (the “*B-BBEE Act*”) is the primary legislation through which this B-BBEE policy is implemented. In terms of the B-BBEE Act, B-BBEE consists of measures and initiatives that are aimed at:

- increasing levels of equity ownership by black people in businesses operating in South Africa;
- increasing the number of black people who participate in management roles in business;
- improving the skills of black employees;
- assisting small and medium-sized businesses that are majority-owned by black people;
- procuring goods and services from businesses that are good contributors to B-BBEE; and
- corporate social investment and development.

To aid the South African government in assessing the state of transformation of publicly listed companies, the B-BBEE Act, read together with the B-BBEE Regulations, requires that all companies listed on the JSE and government entities report to the B-BBEE Commission annually on their compliance with B-BBEE.

Other sector-specific reporting regulations include the Consumer Protection Act, No 68 of 2005, which requires the establishment of national norms and standards relating to consumer protection that promote a fair, acces-

sible and sustainable marketplace, including consumer education concerning the social and economic effects of consumer choices.

An important legislative development is the introduction of the Climate Change Act, No 22 of 2024, which was assented to by the President on 23 July 2024 and, save for certain sections therein, came into operation on 28 February 2025. The purpose of the Climate Change Act is to, inter alia, enable the development of an effective climate change response and a long-term, just transition to a low-carbon and climate-resilient economy and society for South Africa in the context of sustainable development.

Sustainability Reporting/ESG Guide

A significant development in the field of ESG is the publication of the second Code for Responsible Investing in South Africa (CRISA 2) by the CRISA Committee. The first Code for Responsible Investing in South Africa (CRISA) was published in 2011 and aimed to encourage institutional investors and service providers to incorporate ESG issues into their investment decisions. CRISA 2 builds on CRISA and sets out five voluntary principles for stewardship and investment as a key component of the governance framework in South Africa. CRISA 2 has since been endorsed by various institutions, including the FSCA.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies and functions involved in the governance and management of a company in South Africa are as follows.

The Board of Directors

The Companies Act entrusts the board of directors with the authority to direct and regulate the business and affairs of the company, save to the extent that the Companies Act or the MOI provides otherwise. The board can delegate functions to individual directors, committees, management and employees.

The Company Secretary

A public company or state-owned company is required to appoint a company secretary in terms of the Companies Act and the Listings Requirements. A company secretary must maintain independence from the board and, amongst other activities, is tasked with providing guidance to the board on their roles, responsibilities and powers, compliance with applicable laws and the company's MOI.

Prescribed Officers

The Companies Act and Regulations include the concept of a prescribed officer. A prescribed officer is a person who:

- exercises general executive control over, and management of the whole or a significant portion of, the business and activities of the company; or
- regularly participates to a material degree in the exercise of general executive control over and management of the whole, or a significant portion, of the business and activities of the company.

Prescribed officers have the same fiduciary responsibilities as directors – notably, a responsibility of care, skill and diligence and the duty to avoid conflicts of interest. Alongside directors, prescribed officers can be held personally liable for breaching their duties.

Social and Ethics Committee (SEC)

These committees are statutory governance structures in South African company law governed by the Companies Act and the Regulations. The SEC is not a sub-committee of the board and therefore does not enjoy all of the common law powers that a sub-committee of the board would otherwise enjoy. It is, however, entitled to require any information or explanation from any director or prescribed officer, and may:

- request from any employee any information or explanation necessary for the performance of its functions;
- attend any annual general meeting (AGM) of shareholders and receive all notices and other communications relating thereto; and
- be heard at AGMs on any part of the business of the meeting that concerns the committee's functions.

Its functions are limited to those set out in the Regulations, which are, inter alia:

- to monitor the company's activities, having regard to any relevant legislation, other legal requirements or prevailing codes of best practice;
- to ensure good corporate citizenship;
- to draw matters within its mandate to the attention of the board as occasion requires; and
- to report, through one of its members, to the shareholders of a company at the AGM on the matters within its mandate.

The Companies Amendment Act has amended the Companies Act by introducing key provisions governing SECs. In terms of the composition requirements, an SEC must comprise no fewer than three members (ie, not limited to directors); in the case of public and state-

owned companies, the majority of the members must be non-executive directors and must have been non-executive directors during the previous three financial years and, in the case of any other company, the members must consist of no fewer than three directors or prescribed officers, at least one of whom must be a non-executive director and who must have been a non-executive director within the previous three financial years.

In addition, public and state-owned companies must appoint their SECs at each AGM and, for other companies required to have an SEC (ie, private companies with a public interest score (PI Score) in excess of 500), the SEC must be appointed annually by the board of directors.

Public and state-owned companies must now also present an SEC report to their shareholders at their AGMs or annually at a shareholders meeting, or with a resolution as contemplated in Section 60 (ie, round robin resolutions).

Shareholders

Ownership and control of a company vests with the shareholders, whose primary governance role relates to monitoring and holding the board accountable (see 3.2 Decisions Made by Particular Bodies, 3.3 Decision-Making Processes, 5.1 Relationship Between Companies and Shareholders and 5.2 Role of Shareholders in Company Management for further details).

Other Stakeholders

King IV endorses “*stakeholder-inclusive approach*”, in which the board takes into account the legitimate and reasonable needs, interests and expectations of all material stakeholders in exercising its duties in the best interests of the organisation. Employees are viewed as a key constituency of a company and are afforded

the right to apply to a court in order to prevent a company from doing anything inconsistent with the Companies Act, and a trade union or employee representative may invoke the statutory derivative action.

3.2 Decisions Made by Particular Bodies

A company's MOI ordinarily designates the decision-making powers to the board of directors (although there are some decisions that are reserved for shareholder consideration). The main decisions made at each level of the management of the company are as follows.

- The board of directors – the board makes the majority of decisions customarily related to a company's strategy and general management. In this regard, the business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that the Companies Act or the company's MOI provides otherwise.
- Management – in instances where the board of directors is different to the management team, the latter will make decisions on a company's day-to-day operations within the ambit of the powers delegated to management by the board.
- The shareholders – in accordance with the Companies Act, there are a number of decisions that are specifically reserved for shareholders and that can only be passed by either a special or ordinary shareholder resolution (see 3.3 Decision-Making Processes for further details). A company's MOI might include matters in addition to those required in terms of the Companies Act. In certain instances, the shareholders' approval relates to decisions of directors.

3.3 Decision-Making Processes

The board of directors, management team and shareholders ordinarily make decisions in the following ways.

The Board of Directors

The board acts through board resolutions and makes decisions by a majority vote, with each director normally carrying one vote, although this may be varied in the MOI. Board meetings must be called on reasonable notice, and the quorum necessitates the presence of a majority of directors at the meeting. It is important to note that a company's MOI may require unanimous or another consent threshold, if the default position (ie, the majority requirement) in the Companies Act is altered. Moreover, instead of holding a board meeting, the board can make decisions via "round robin" written resolutions, which require approval by a majority of directors of the subject matter of the round robin resolutions. These resolutions generally have the same status as if passed at a meeting of the board.

The board of directors may appoint as many committees as it deems necessary and assign any of its authority to them (while maintaining ultimate accountability for their decisions and conduct). Please see 1.2 Sources of Corporate Governance Requirements regarding the mandatory committees to be appointed by public companies.

Management

The management team implements board decisions within its delegated and prescribed authority. Management may include prescribed officers of a company (see 3.1 Bodies or Functions Involved in Governance and Management).

The Shareholders

The following matters require shareholder approval by a special resolution (generally by 75% of shareholders, although the threshold may be higher or lower if specified in terms of a company's MOI, provided it must be 10% higher than the threshold for an ordinary resolution):

- amending the MOI, or ratifying a consolidated revision thereof;
- ratifying ultra vires acts by the board;
- providing financial assistance to directors or to related companies (such as group companies);
- providing financial assistance to acquire securities of the company or of a related company (the Companies Amendment Act has amended the Companies Act so that Section 45, which governs financial assistance, no longer applies to the giving by a company of financial assistance to or for the benefit of its subsidiaries);
- approving certain “*fundamental transactions*” such as major asset disposals, schemes of arrangement or statutory mergers/amalgamations;
- certain issues of shares, securities or options;
- certain share repurchases;
- remunerating directors in that capacity; and
- winding up the company on a voluntary basis.

Shareholders must approve the appointment of auditors and an audit committee where applicable, by way of an ordinary resolution (generally 50% plus one vote). A company's MOI may stipulate particular “*reserved matters*” that can only be considered after shareholder approval. Moreover, the Listings Requirements require shareholder approval before the implementation of certain transactions, either by ordinary resolution (eg, a category 1 major transaction) or by special resolution (eg, a share buy-back). The

approval threshold of JSE-listed companies for special resolutions is 75% and 50% for ordinary resolutions.

4. Directors and Officers

4.1 Board Structure

South African company law provides for a single-tier, unitary board structure. The Companies Act does not distinguish between executive and non-executive directors, and both are full board members. King IV does, however, distinguish between and recommend specific roles for executive and non-executive directors.

In terms of the Companies Act, a private company or personal liability company must have a minimum of one director, whereas a public, a non-profit and a state-owned company must have a minimum of three directors. Certain industries, such as the banking and financial sector, may impose additional governance requirements on boards.

King IV recommends that the governing body (ie, the board of directors) should assume responsibility for its composition, including setting out the processes required for it to achieve the appropriate balance of knowledge, experience, skills, independence and diversity to effectively and objectively perform its governance responsibilities. King IV recommends that the board should consist of a majority of independent non-executive members.

In determining the required number of board members, King IV recommends that the board considers, inter alia:

- the appropriate mix of executive, non-executive and independent non-executives;

- diversity; and
- the need for a sufficient number of members that qualify to serve on the committees of the board.

In relation to committees, King IV recommends an audit committee (which is a statutory requirement for some companies), a nominations committee, a risk governance committee, a remuneration committee and a social and ethics committee. The audit committee is primarily responsible for providing independent oversight of the integrity of the annual financial statements (AFS). The nominations committee is primarily responsible for the process of nominating, electing and appointing the board of directors.

4.2 Roles of Board Members

Position Under King IV

King IV recommends that the board of directors comprises a combination of executive, non-executive and independent non-executive directors. As a minimum requirement, King IV recommends that a chief executive officer (CEO) and one other executive – for example, a chief financial officer (CFO) – should be appointed to the board of directors of a company so as to ensure that the board of directors has more than one point of direct contact with management.

In addition to the role of CEO (and CFO), it is recommended that the board of directors elects an independent non-executive director as chair to lead the board of directors in the effective and objective discharge of their governance role and responsibilities. The CEO leads the implementation and performance of a board-approved strategy and policies, and should serve as the main link between management and the board of directors.

4.3 Board Composition Requirements/Recommendations

The Companies Act prescribes a minimum number of directors for private and public companies, as set out in **4.1 Board Structure**. A company's MOI may require a higher number of directors than the minimum number required by the Companies Act.

King IV recommends that a board of directors should possess the appropriate mix of skill, knowledge, expertise and experience, including the business, industry and commercial experience needed to govern a company (see **4.1 Board Structure** for further details).

B-BBEE

B-BBEE encourages companies to constitute diverse boards of directors as this has an impact on a company's ability to conduct business or conclude contracts with the state or state-owned companies (see **2.2 ESG Considerations** for further details on B-BBEE).

4.4 Appointment and Removal of Directors/Officers

Position Under the Companies Act

Appointment of directors

Directors are generally elected to the board by a majority vote of the shareholders. The company's MOI can allow directors to be appointed directly by any party specified in it, or it can allow directors to serve as ex officio directors. The Companies Act specifically provides that at least 50% of the directors of a profit company (ie, a company incorporated for purposes of financial gain for its shareholders) must be elected by shareholders.

Removal of directors

In terms of the Companies Act, directors can resign or be removed by shareholders or the remainder of the board.

Shareholder removal

The Companies Act contains an unalterable provision for the removal of directors from the board by an ordinary resolution of shareholders at a general meeting. Before this resolution is considered by the shareholders, the director(s) concerned must be given proper notice of the proposed meeting and the resolution, and the director(s) must be afforded a reasonable opportunity to make a presentation to the shareholders, either in person or through a representative.

Board removal

If a director becomes incapacitated, ineligible or disqualified, or has neglected or been derelict in the performance of their duties, the board will be able to remove the director in question. A company's MOI may indicate additional processes for the removal of a director.

A shareholder, director, prescribed officer or company secretary can also approach the High Court to remove a director by:

- invoking the oppression remedy in terms of the Companies Act; or
- having a director declared a delinquent in accordance with the Companies Act, if they are in material or gross breach of their duties.

The Second Amendment Act has amended the Companies Act to extend the time bar to declare a director delinquent from 24 to 60 months. This amendment further grants the court discretion to extend the period in respect of which proceedings to recover any loss, damages or costs may be commenced, which is currently within three

years after the act or omission that gave rise to the liability.

4.5 Rules/Requirements Concerning Independence of Directors

Position Under the Companies Act

Conflicts of interest

Avoiding a conflict of interest is one of the central fiduciary duties of a director. The Companies Act provides that a director who has a material/substantial personal financial interest in a matter before the board, or who knows that "*related person*" has an interest, must disclose such interest to the board and recuse themselves from board deliberations on that matter. Family members within specific degrees of consanguinity or affinity, second entities of which the contemplated director is also a director, and organisations under the director's control or influence are all regarded as "*related persons*".

In relation to the audit committee of a public or state-owned company, the test for independence under the Companies Act is that the director must not be:

- involved in the day-to-day management of the company's business nor have been so involved at any time during the previous financial year;
- a prescribed officer or full-time employee of the company and must not have held such office during the previous three financial years;
- a material supplier or customer of the company such that a reasonable and informed third party would conclude that the director's integrity, impartiality or objectivity is compromised by that relationship; or
- related to any person who falls within any of the above categories.

If the company appoints an audit committee with persons not considered “*independent*” in terms of the Companies Act, any functions undertaken by such audit committee will be considered as not having been performed by a suitably constituted audit committee.

Position Under King IV

Independence and conflicts

King IV recommends that a majority of the company’s non-executive directors should be independent and that the chair of the board should be independent. King IV sets out certain factors to consider when determining whether a director is considered “*independent*”, including whether:

- the director holds any equity interest in the company or group that is material to their personal wealth;
- the director holds directorships on a number of other group companies;
- the director is a material lender or financier to the company; or
- the director’s remuneration is in any way based on the performance of the company.

Position Under the Takeover Regulations

The Takeover Regulations (Chapter 5 of the Regulations) (the “*Takeover Regulations*”) require an independent board to be established in certain circumstances in relation to affected transactions, which include certain fundamental transactions, such as major disposals, schemes of arrangement and mergers, as well as the acquisition of control of a regulated company.

4.6 Legal Duties of Directors/Officers

Directors and prescribed officers are subject to a number of duties under both the Companies Act and the common law. These duties can be traditionally categorised into two groups:

- fiduciary duties; and
- the duty of care, skill and diligence.

Position Under the Companies Act and the Common Law

Fiduciary duties

The Companies Act, in part, codified the common law principles regulating fiduciary duties and mandates that all directors, alternate directors, prescribed officers and members of board or audit committees must, amongst other things:

- exercise their powers and functions in good faith, for a proper purpose, and in the “*best interests of the company*”;
- disclose personal financial interests in certain instances; and
- not use their office or position to secure an advantage or knowingly cause harm to the company.

Directors remain subject to their common law fiduciary duties to the extent that the Companies Act does not specifically deal with particular duties. These common law duties encompass the fiduciary duties to:

- act within designated powers;
- maintain and exercise unfettered discretion and independent judgement; and
- avoid conflicts of interest.

Each director should act with the degree of care, skill and diligence that may reasonably be expected of a person:

- carrying out the same functions in relation to the company as those carried out by that director; and
- having the general knowledge, skill and experience of that director.

4.7 Responsibility/Accountability of Directors

Under South African law, directors owe their fiduciary duties and the duty to act with reasonable care, skill and diligence to the company (this entails acting only in the bona fide interests of the company and its shareholders as a body). Directors as such owe no fiduciary duty to the shareholders individually.

Furthermore, King IV endorses a stakeholder inclusive model (or enlightened shareholder value approach), in terms of which the needs and interests of stakeholders should be taken into account by the board, alongside those of the shareholders.

Directors do not owe fiduciary duties to third parties and creditors; however, the Companies Act provides that a company may not trade recklessly, with gross negligence or with the intent to defraud any creditors. In the event of a breach of the relevant provisions of the Companies Act, directors may be held personally liable to creditors or other third parties where loss or damage was suffered as a result of the transgression.

4.8 Consequences and Enforcement of Breach of Directors' Duties

The Companies Act provides, inter alia, that a director may be held responsible in accordance with;

- the principles of the common law relating to breach of a fiduciary duty, for any loss, damages or costs sustained by the company as a consequence of any breach by the director of their duties; or
- the principles of the common law relating to delict for any loss, damages or costs sustained by the company as a consequence of any breach by the director of their duty of

care, skill and diligence, certain other provisions of the Companies Act, or any provision of the company's MOI.

Note that the liability above – eg, for a breach of a fiduciary duty by the director – is to the company and not to third parties under the Companies Act. This is consistent with the principle of reflective loss, which has recently been reaffirmed in South African courts. In other words, where a company suffers loss caused by a breach of duty owed to it, only the company may sue in respect of that loss, and a shareholder does not have the right to claim for a reduction in the value of its shares as this loss merely reflects the loss suffered by the company itself as the result of wrongdoing (see 5.4 Shareholder Claims (Statutory Derivative Action)).

Furthermore, defaulting directors are jointly and severally liable to the company for any loss. The Companies Act provides a legal avenue to pursue an action on behalf of a company in order to recover losses associated with a breach of directors' legal duties (further details on such actions are set out in 5.4 Shareholder Claims).

4.9 Other Bases for Claims/Enforcement Against Directors/Officers Position Under the Companies Act

A director is liable for any loss, costs or damages suffered by a company as a direct or indirect consequence of a director, inter alia, having:

- acted on behalf of the company without the requisite authority, despite knowing that they lacked the authority to do so;
- acquiesced in the reckless trading of the company's business;
- engaged in conduct calculated to defraud stakeholders; or

- been party to false or misleading communications in financial statements and/or in a prospectus.

Directors may be subjected to criminal penalties in limited circumstances, with stricter consequences designated for offences including false statements or reckless behaviour.

Directors may not be relieved of any legal duties, liabilities or any legal consequences arising from an act or omission constituting wilful breach of trust or wilful misconduct on the part of a director negated or limited by virtue of a company's MOI, any agreement or any resolution of a company.

Limitation of Liability

Business judgement rule

The Companies Act provides for the business judgement rule, which is a protective and defensive mechanism for directors who face liability for potential breaches of their legal duties (see **4.6 Legal Duties of Directors/Officers** for further discussion).

In terms of the Companies Act, the defence is available to a director (other than for breaches of duties of good faith) if the following requirements are met:

- the director took reasonably diligent steps to become informed about the matter at hand;
- the director had no material personal financial interest in the subject matter of the decision, and had no reasonable basis to know that any related person had a personal financial interest in the matter, or had dealt with those personal financial interests as required by law; and
- the director made a decision, or supported the decision of a committee or the board, with

regard to that matter, and the director had a rational basis for believing, and did believe, that the decision was in the best interests of the company.

Director's indemnity insurance

Companies are prohibited from providing indemnity or insurance to a director for wilful misconduct or for a wilful breach of trust. Nevertheless, on a case-by-case basis, the company may indemnify its directors, or purchase insurance policies that safeguard directors in the event that they have contravened their legal duties in a non-wilful manner. This is subject to certain restrictions – for example, a company is prohibited from indemnifying or insuring its director for:

- fines arising from criminal offences;
- reckless or fraudulent trading; or
- acting without proper authority.

A director is allowed to obtain insurance against personal liability. If a company obtains the requisite approvals, it may also pay the insurance premium for the directors.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Position Under the Companies Act

The Companies Act provides that, except to the extent provided otherwise by a company's MOI, directors may be remunerated for their services (as director) subject to the passing of a special resolution of shareholders, which in turn must be approved two years prior to such remuneration being paid.

The Companies Act also specifies certain matters that require shareholder approval so as to limit benefits that may go to directors and prescribed officers, such as:

- an issue of shares if the class of shares being issued (including as a result of a transaction or series of transactions) will be equal to or exceed 30% of the voting power of all the shares of that class held by shareholders immediately held before the transaction(s);
- a decision by the board determining that the company may acquire a number of its own shares; and
- a decision by the board for the company to provide financial assistance to a director or prescribed officer.

Listings Requirements and King IV

The Listings Requirements have endorsed the King IV recommendation that shareholder approval in respect of remuneration is to be pursued as follows: where either the remuneration policy or the implementation report, or both, were voted against by 25% or more of the non-binding advisory voting rights exercised at the AGM, King IV advocates that the following should be disclosed in the background statement of the remuneration report succeeding the voting:

- persons whom the company engaged, and the manner and form of engagement to ascertain the motives for dissenting votes; and
- the nature of steps taken to address legitimate and reasonable objections and concerns.

It should also be noted that the Companies Amendment Act has introduced the requirement for state-owned and public companies to present a remuneration policy and remuneration report.

Consequences for Failing to Comply With Approval Requirements

The company may not pay remuneration to its directors for their service as directors, except to the extent that the MOI provides otherwise. Remuneration may be paid only in accordance with a special resolution approved by the shareholders within the previous two years (note that this is not salary but payments to directors for their services as such). If the board of a company proceeds to remunerate its directors without first obtaining the requisite shareholder approval, such payment is unlawful (see 4.6 Legal Duties of Directors/Officers for further discussion) and could be liable to the company for any loss, damages or costs suffered by the company as a result. The shareholders could challenge the board decisions relating to director remuneration (see 5.4 Shareholder Claims and 4.4 Appointment and Removal of Directors/Officers for further discussion).

4.11 Disclosure of Payments to Directors/Officers

A company that is required to have its AFS audited in terms of the Companies Act (ie, public companies, state-owned companies and private companies with a PI Score in excess of 350) must disclose all remuneration and other benefits paid to its directors and prescribed officers in its AFS. This should be done on an individualised basis.

Furthermore, the Companies Act requires that the AFS of a company contain the following particulars relating generally to directors and prescribed officers:

- their remuneration and benefits received;
- the amount of any pensions paid to them by the company;

- any amount paid or payable by the company to a pension scheme;
- the amount of any compensation paid to them in respect of loss of office;
- the number and class of any securities issued to them, and the consideration received by the company for those securities; and
- details of their service contracts.

All remuneration paid to or receivable by a director or prescribed officer must be disclosed. This encompasses not only the remuneration paid to or received by the director or prescribed officer for services to the company, but also all other remuneration received by the director or prescribed officer for services rendered as a director or prescribed officer to any other company within the same group of companies.

Companies Amendment Act

Another amendment to the Companies Act introduced by the Companies Amendment Act relates to access to information. In this regard, section 26 (1) sets out a list of company records a beneficial interest holder (which includes a shareholder) is entitled to inspect and copy, which has been expanded to include a company's register of the disclosure of beneficial interest. A beneficial interest holder will therefore have the right to inspect and copy information from a company's MOI, the records in respect of a company's directors, reports to annual meetings, notices and minutes of annual meetings, securities register, register of the disclosure of beneficial interests and a company's AFS.

Moreover, the Companies Amendment Act has amended Section 26 (2) of the Companies Act by granting non-beneficial interest holders (ie, non-shareholders) the right to inspect and copy a company's AFS, MOI, director records and beneficial interest register. However, it should be

noted that the right afforded to non-beneficial interest holders to inspect and copy a company's AFS does not apply to a private company, a non-profit company or a personal liability company wherein an AFS is internally prepared in a company with a PI Score of less than 100 or is independently prepared in a company with a PI Score of less than 350.

Related to the above, the Companies Amendment Act has also amended the Companies Act so that companies that are required to have their AFS audited must include in their AFS the remuneration and benefits received by each individual director and prescribed officer, each of whom must be named.

The Companies Amendment Act has further amended the Companies Act so that public and state-owned companies must prepare and present a remuneration policy and remuneration report. The remuneration policy must be presented to and approved by a company's shareholders at the AGM by an ordinary resolution and, if not approved, must be presented at the next AGM or at a shareholders' meeting called for such purpose. If approved, the remuneration policy will remain in force for three years from approval and must be approved every three years thereafter. It should be noted that the remuneration policy may be amended prior to the end of the three-year period, provided that any material amendment can only be implemented after it is approved by the shareholders by an ordinary resolution at a shareholders' meeting called for this purpose or at an AGM.

The remuneration report must consist of a background statement, a copy of the company's remuneration policy and an implementation report. The implementation report must include details of the total remuneration received by each

director and prescribed officer in the company, the total remuneration in respect of the employee with the highest total remuneration, the total remuneration in respect of the employee with the lowest total remuneration in the company, and the average total remuneration of all employees, median remuneration of all employees and the remuneration gap reflecting the ratio between the total remuneration of the top 5% highest paid employees and the total remuneration of the bottom 5% lowest paid employees of the company (also referred to as the “*wage gap*”).

The remuneration report must be prepared each year in respect of the previous financial year for presentation and approval at the AGM; if not approved at the AGM, then the remuneration committee (“*Remco*”) must, at the next AGM, present an explanation on the manner in which the shareholders’ concerns have been taken into account, and the non-executive directors serving on the Remco must stand for re-election as members of the Remco at the AGM at which the explanation is presented.

If at the AGM in the year immediately following the year contemplated above, the remuneration report in respect of the previous financial year is also not approved by an ordinary resolution of shareholders, then the non-executive directors who serve on the Remco may continue to serve as directors, provided they successfully stand for re-election at that AGM and will not be eligible to serve on the Remco for a period of two years thereafter.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The relationship between the company and its shareholders is statutory and contractual in nature, as it is generally regulated by the Companies Act and the company’s MOI, which generally sets out rights attaching to shares. The relationship between shareholders and the company may also be regulated by a shareholders’ agreement but the shareholders’ agreement must be consistent with the company’s MOI; any provision that is inconsistent with the MOI is void to the extent of such inconsistency.

Generally, the principle of separate legal personality entails that shareholders are not liable for the company’s acts or omissions. Shareholders do not owe any legal duties under the common law or the Companies Act to the company.

Only in exceptional circumstances can a court impose personal liability on shareholders who have flouted the common law principle of separate corporate personality, or the court may invoke the Companies Act’s statutory mechanism to pierce the corporate veil in cases of “*unconscionable abuse*” of a company’s separate legal personality.

Shareholders are entitled to a share of the company’s distributed profits in proportion to their respective shareholdings and, in the event of a company winding-up, to the surplus assets after the company’s creditors have been fully paid. Typically, preference shareholders are entitled to receive their respective portions before ordinary shareholders upon the winding-up of a company.

5.2 Role of Shareholders in Company Management

Position Under the Companies Act

As mentioned in 4.4 **Appointment and Removal of Directors/Officers**, shareholders are responsible for the appointment of a certain percentage of directors to the board of a company. As set out in 4.2 **Roles of Board Members**, the management of a company is primarily done by the directors but, in addition to matters and actions that require shareholder approval in accordance with the Companies Act provisions, a company's MOI may set out certain actions that may not be carried out unless approved by a majority of shareholders. Such actions are generally known as reserved matters.

The Companies Act enables shareholders to perform their duty of oversight by allowing them to invoke their right to a statutory derivative action (see 5.4 **Shareholder Claims** for further discussion). This statutory derivative action can also be brought against any third parties who have committed any wrongdoing towards the company.

5.3 Shareholder Meetings

Position Under the Companies Act

The Companies Act provides that a public company must convene an AGM initially no more than 18 months after the company's incorporation, and thereafter must convene one annually (and within 15 months after the preceding year's AGM). AGMs are not required for private corporations; however, they are commonly included in the company's MOI.

At a minimum, the following matters must be covered at an AGM of a public company:

- the presentation of the directors' report, the audited financial statements of the company

for the immediately preceding financial year, an audit committee report, an SEC report and a remuneration report;

- the election of any directors, to the extent required by the Companies Act or the company's MOI;
- the appointment of the company's auditor for the ensuing financial year, an audit committee (in the case of public and state-owned companies only) and an SEC; and
- any other issue presented by shareholders, irrespective of whether the company was given notice of the subject matter.

Furthermore, shareholders' meetings may be convened to deliberate on specific company matters, such as the approval of a fundamental transaction, as and when requisitioned by the board, a person indicated in the company's MOI or rules, or shareholders who, in aggregate, hold at least 10% of the voting rights entitled to be exercised on the subject matter to be voted on (except where a court decides that the subject matter in question is frivolous or vexatious, or has already been decided by shareholders).

Any general meeting of shareholders can be conducted entirely or partially by electronic communication, provided that the electronic medium allows all shareholders to participate reasonably effectively as set out in the Companies Act.

Default positions

In terms of the Companies Act, the following are the default or standard positions, which can be altered by the company's MOI:

- for a public and non-profit company, the notice period is 15 business days (in any other case, the notice period is ten business days);

- the quorum prerequisite for shareholders' meetings for any company is shareholders representing at least 25% of the total votes exercisable at the meeting, whether the shareholders are physically present or represented by proxy;
- at minimum, three shareholders must be present in person or by proxy, if the company has three or more shareholders;
- in the event that a quorum is not attained at the first assembly, the meeting will be postponed by a week and those present at the postponed meeting will be considered to comprise a quorum; and
- for JSE-listed companies, the Listings Requirements permit round robin resolutions for very limited shareholder decisions only, and the balance of shareholder decisions must be approved at general meetings.

The board of a company, or any other person specified in the company's MOI or rules, may call a shareholders' meeting at any time. The board of directors must call a shareholders' meeting if a shareholder with a holding of at least 10% of the voting rights, or a group of shareholders with a combined such holding, demands the board to convene a shareholders' meeting to discuss a specific issue, or if demands are made for substantially the same purpose. If the board fails, the shareholders may pursue an order of the court. Moreover, any two shareholders can require that the company includes particular proposed resolutions on the agenda of a meeting demanded as aforesaid or at the next shareholders' meeting or by round robin.

5.4 Shareholder Claims

Position Under the Companies Act

In terms of the Companies Act, a shareholder may seek judicial relief if they have been subjected to oppressive or prejudicial conduct due

to, inter alia, any act or omission of a company, or due to the exercise of a director's powers, and a court may make any order it deems appropriate, including an order restraining the conduct complained of or setting aside an agreement or transaction.

Furthermore, shareholders may approach the court for any order sufficient to safeguard any of their rights or to remedy any harm done to them by:

- the company due to a violation of, inter alia, the Companies Act or the MOI; or
- a director insofar as that director may be liable for a breach of their legal duties.

Moreover, in limited instances, a shareholder may launch an application with the court to impede:

- the company from breaching any provision of the Companies Act; or
- the company or the directors from violating any constraint included in the MOI regarding the company's capacity or the directors' authority.

A claim for damages may also be brought by shareholders who have endured a loss due to a breach of the Companies Act by directors.

Statutory Derivative Action

The Companies Act empowers shareholders to mandate a company to institute legal proceedings, or take related steps, to protect the legal interests of the company. However, within 15 business days a company may launch an application to set aside the shareholders' demand only on the grounds that it is frivolous, vexatious or devoid of merit.

5.5 Disclosure by Shareholders in Publicly Traded Companies

The amendments to the Companies Act introduced by the GLAA (see below) have inserted the definition of an “*affected company*”, which essentially means a regulated company and a private company that is controlled by or is a subsidiary of a regulated company.

In terms of Section 122, a person must notify an affected company in the prescribed manner and form within three business days after that person:

- acquires a beneficial interest in sufficient securities of a class issued by that company such that, as a result of the acquisition, the person holds a beneficial interest in securities amounting to 5%, 10%, 15% or any further whole multiple of 5% of the issued securities of that class; or
- disposes of a beneficial interest in sufficient securities of a class issued by a company such that, as a result of the disposition, the person no longer holds a beneficial interest in securities amounting to a particular multiple of 5% of the issued securities of that class.

Upon having received such notice, an affected company must file a record of that notice with the CIPC.

Upon receiving such notice, a regulated company must:

- file a copy with the Takeover Regulatory Panel (TRP); and
- report the information to the holders of the relevant class of securities, unless the notice concerned a disposition of less than 1% of the class of securities.

The Takeover Regulations require a mandatory offer to be made to the remaining shareholders when a party (operating alone or in concert) acquires securities in a regulated company that increase the acquiring party’s beneficial interest in the voting rights of such company to 35% or more.

Amendments to the Companies Act Brought About by the GLAA

As discussed in 2.1 Hot Topics in Corporate Governance (Greylisting of South Africa), the Companies Act has been amended by the GLAA to include the definition of “*beneficial owner*”, which means, in respect of a company, a natural person who, directly or indirectly, ultimately owns or exercises effective control of that company, including through:

- the holding of beneficial interests in the securities of that company;
- the exercise of, or control of the exercise of, the voting rights associated with securities of that company;
- the exercise of, or control of the exercise of, the right to appoint or remove members of the board of directors of that company;
- the holding of beneficial interests in the securities, or the ability to exercise control, including through a chain of ownership or control, of a holding company of that company;
- the ability to exercise control, including through a chain of ownership or control, of, inter alia, a juristic person other than a holding company of that company; or
- the ability to otherwise materially influence the management of that company.

It is important to note here that the concept of “*beneficial interest*” pre-dates the GLAA and was therefore already in the Companies Act and is distinct from beneficial ownership. When used

in relation to a company's securities, "*beneficial interest*" means the right or entitlement of a person, through ownership, agreement, relationship or otherwise, alone or together with another person, to:

- receive or participate in any distribution in respect of the company's securities;
- exercise or cause to be exercised, in the ordinary course, any or all of the rights attaching to the company's securities; or
- dispose or direct the disposition of the company's securities or any part of distribution in respect of the securities.

It does not include any interest held by a person in a unit trust or collective investment scheme in terms of the Collective Investment Schemes Act, 2002 (Act 45 of 2002).

The distinction between beneficial ownership and beneficial interest is important as the reporting obligations in relation to beneficial interests are applicable to "*affected companies*", whereas the reporting obligations flowing from beneficial ownership apply to companies that are "*non-affected*".

In this regard, an affected company must establish and maintain a register of the persons who hold beneficial interests equal to or in excess of 5% of the total number of securities of that class issued by the company, together with the extent of those beneficial interests, and must file a copy of its register of the disclosure of beneficial interest with the CIPC, together with its annual return.

On the other hand, a non-affected company must record in its securities register prescribed information regarding the natural persons who are the beneficial owners of the company, and

must also file a record of the beneficial owners with the CIPC.

In certain respects, the guidelines published by the CIPC titled "*User Guidelines Beneficial Ownership*" seem to sometimes conflate beneficial ownership with beneficial interest, even though, as discussed above, these concepts are not one and the same according to the definitions in the Companies Act. In any event, it should be noted that both affected and non-affected companies have reporting obligations and it is advisable to follow the steps to submit beneficial ownership/beneficial interest information as per CIPC's guidelines.

Listings Requirements

The Listings Requirements mandate issuers to disclose shareholdings of 5% or more in their annual report and circulars.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

On an annual basis, a company must prepare AFS within six months after the end of its financial year, or within such shorter period as may be appropriate in accordance with the Companies Act.

The Companies Act provides that the AFS of a public company must be audited and, in the case of profit and non-profit companies, the AFS may:

- be audited if it is in the public interest to do so under the Regulations;
- be audited voluntarily if the company's MOI so provides; or

- be independently reviewed in a manner required by the Companies Act.

The AFS must be approved by the board and be presented to the first shareholders' meeting after the AFS have been approved by the board and generally include the following information:

- a director's report detailing the state of the company; and
- an auditor's report.

The AFS must satisfy financial reporting standards as to form and content if such standards are prescribed.

6.2 Disclosure of Corporate Governance Arrangements

Position Under the Listings Requirements

In addition to the requirements discussed in 6.1 **Financial Reporting**, the Listings Requirements impose a number of ongoing obligations on public companies. As a result, issuers must comply with financial reporting and disclosure requirements in critical areas such as periodic financial information, price-sensitive information, profit forecasts and major company activities.

As per King IV, good governance can be attained through its "*apply and explain*" disclosure framework, which requires a company to:

- apply the recommended practices thoughtfully, with common sense, and proportionally (ie, in line with its size and resources, and the scope and complexity of its operations); and
- provide a descriptive account of that implementation with reference to the recommended standards.

This account, together with the company's AFS (and other external reports), code of conduct and

ethical codes, and integrated reports, should be published on the company's website (or other widely accessible media or platforms).

6.3 Companies Registry Filings

In terms of the Companies Act, all companies (including external companies and close corporations) are required to file annual returns with the CIPC within a specified time period. Companies must file their annual returns within 30 business days after the anniversary date of their registration date, regardless of whether they were active or not. Notably, the amendments to the Companies Act introduced by the GLAA require companies to include a copy of their AFS and a copy of their securities registers in their annual returns and, in the case of affected companies, a copy of the register of disclosure of beneficial interest.

If annual returns are not filed within the specified timeframe, the company may be deregistered as the CIPC will assume that the company is inactive. The deregistration procedure has the legal consequence of terminating the juristic personality of the company or close corporation, with the effect that the company or close corporation ceases to exist.

Furthermore, all entities are required by law to file their taxable returns with the South African Revenue Services to determine their taxable income.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Position Under the Companies Act

The Companies Act prescribes that only certain types of companies require an external auditor to be appointed to audit their financial state-

ments. In terms of the Companies Act, it is mandatory for public and state-owned companies to appoint an auditor and to have their financial statements audited.

The appointment of an auditor must occur upon incorporation of the company by the incorporators, or within 40 business days of incorporation by the directors of the company. The first auditors of a company will hold office until the first AGM of the company, and are re-appointed on an annual basis at every AGM.

An appointed auditor may not be:

- a director, prescribed officer, employee or consultant of the company;
- a director, officer or employee of the person appointed as company secretary;
- a person who habitually or regularly performs the duties of accountant or bookkeeper of the company; or
- a person appointed as the auditor of the company in the immediately preceding five years.

Pursuant to the amendments to the Companies Act, a period of two years must lapse before an auditor can be appointed to a company if an auditor had certain involvement with the company. This is a departure from the previous time period, which was five years.

It is not mandatory for a private or personal liability company to appoint an auditor, unless the company is required to produce audited financial statements (see **6.1 Financial Reporting**).

The Regulations set out a guideline to determine when it is in the public's interest to have the financials of a company audited. The Regulations provide that a private profit company's

financials must be audited if they meet any one of the following criteria:

- if such a company, in the ordinary course of its primary activities, holds assets in a fiduciary capacity for persons who are not related to the company, and the aggregate value of such assets held at any time during the financial year exceeds ZAR5 million;
- any other company whose PI Score in that financial year is 350 or more; or
- any other company whose PI Score in that financial year is at least 100 (but less than 350) and whose AFS for that year were internally compiled.

Certain categories of private, personal liability and non-profit companies that are not subject to audit requirements may be required to have their AFS independently reviewed by an accountant.

If a company is not required to be audited but is not exempt in terms of the Companies Act, its AFS must be independently reviewed.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

King IV

Generally speaking, requirements for directors in connection with the management of risk and internal controls in a company would fall under the general duty of care, skill and diligence under the Companies Act. In addition, King IV recommends that the board of directors of a company appoints a risk committee that will be in charge of overseeing and mitigating all of the company's potential risks. King IV recommends that the risk committee should comprise at least three directors, the majority being non-executive directors. The chair of the committee should be a non-executive director, and the chair of the board

may chair this committee. It is advised that the committee generates reports that are reviewed and signed by the whole board as acknowledgment that their duties have been appropriately performed in this respect.

King IV emphasises the board's role in risk and opportunity oversight, proposing that the risk committee's membership intersects with that of the audit committee for greater efficiency, and that the meeting agenda should address audit, risk and opportunity as distinct agenda items if the risk and audit roles are integrated in a single committee.

SOUTH KOREA

Law and Practice

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Lee & Ko



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Lee & Ko has an M&A team of approximately 150 attorneys. The firm provides comprehensive legal services for various types of M&A transactions, including those involving financial institutions, privatisations of public corporations, tender offers, corporate mergers/spin-offs and restructuring through the conversion of holding companies. The team works across many industries, including finance, energy, chemicals, food, medical, broadcasting, technology, enter-

tainment and start-ups. By collaborating with other practice groups such as tax, labour, anti-competition and regulatory compliance, Lee & Ko provides clients with a seamless, one-stop service throughout the entire M&A process. The firm's offices in Beijing, Ho Chi Minh City and Hanoi also provide M&A-related legal services. The M&A team has handled significant deals across all industry sectors both domestically and internationally.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

There are five types of corporate/business organisations in Korea, as follows.

- Joint stock company (*chusik hoesa*) – similar to a corporation in the United States, this is the most commonly seen form of corporate/business organisation in South Korea. A joint stock company secures its capital and assets by issuing stocks, and shareholders are liable only to the extent of their investment (ie, they have limited liability), and also have equity rights in the company based on the number of shares they hold.
- Limited company (*yuhan hoesa*) – like a joint stock company, the members of a limited company (equivalent to the shareholders in a joint stock company) are liable only to the extent of their contributions, but the set-up process is simpler and the units (equivalent to the shares in a joint stock company) are not freely transferable, making it suitable for smaller corporate/business organisations.
- Limited liability company (*yuhan chaekim hoesa*) – this is a company where unitholders can directly participate in management while each bears legal responsibility up to the amount that they invested. However, use of this form of company is rare due to (i) its lack of any meaningful benefits compared to a joint stock company and limited company, and (ii) a general lack of familiarity with this type of entity in the market, as it is a relatively new form of corporate/business organisation created in 2012.
- Unlimited partnership (*hapmyung hoesa*) – here, each member, who is also a shareholder, assumes unlimited liability in proportion to their shareholding, and has the author-

ity to execute the company's business and represent the company, making it suitable for joint business ventures among closely related individuals such as family members, relatives or close friends.

- Limited partnership company (*hapja hoesa*) – this type of company has members who bear unlimited liability and members who bear limited liability up to the amount of their investment. Those with unlimited liability manage the business and members with limited liability provide capital and participate in the distribution of profits generated by the business.

According to a survey published by the National Tax Service, approximately 94% of companies in South Korea are joint stock companies. The following guide therefore uses these as context.

1.2 Sources of Corporate Governance Requirements

The primary sources of law governing corporate governance in South Korea are as follows.

Korean Commercial Code (KCC)

The KCC is the most fundamental law relating to corporate governance, which applies to both publicly traded and private companies. The KCC comprehensively regulates all aspects of corporate governance, such as the formation, decision-making, and dissolution of companies. It takes precedence over civil law with respect to corporate governance. However, for publicly traded companies, the Financial Investment Services and Capital Markets Act take precedence over the KCC.

Financial Investment Services and Capital Markets Act (FISCMA)

From a corporate governance perspective, the FISCMA provides for requirements around public disclosure, audit committees, outside

directors and insider trading. It is mandatory for publicly traded companies to comply with listing rules, including those derived from the FIS-CMA and the applicable listing rules of the Korea Exchange (eg, KOSPI Market Listing Rules and KOSDAQ Market Listing Rules).

Act on External Audit of Stock Companies (External Audit Act)

The External Audit Act is a crucial legal framework that mandates companies to undergo external audits and prescribes essential matters related to accounting management for companies subject to external audits and the auditing process conducted by external auditors. It ensures transparency, maintains investor trust and upholds corporate integrity by verifying a company's financial health and the appropriateness of its financial reports. Please refer to Section 6.1 Financial Reporting for details on the External Audit Act.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Various corporate governance requirements for publicly traded companies are provided by the KCC and FISCMA, as well as listing rules for the Korea Exchange (KRX), including the following.

Appointment of Outside Directors and Statutory Auditors

Listed companies are required to appoint at least one-quarter of the total number of their directors as outside directors (ie, independent directors). Publicly traded companies with total assets equal to or above KRW2 trillion must have three or more outside directors, and a majority of the total number of directors must be outside directors. Furthermore, the individuals that have been involved in the company's business activities within the preceding three-year period cannot

be appointed outside directors. The total tenure of outside directors cannot exceed nine years.

Regarding statutory auditors, publicly traded companies with total assets equal to or above KRW100 billion must appoint a full-time auditor or establish an audit committee to oversee the company's affairs and accounting practices, and publicly traded companies with total assets equal to or above KRW2 trillion must set up an audit committee. Individuals appointed as auditors or audit committee members must meet specific qualifications, as stipulated under the KCC.

Corporate Governance Report

Listed companies above a certain size are required to disclose corporate governance reports in accordance with the Corporate Governance Report Guidelines issued by the KRX.

Corporate governance reporting was voluntary when first introduced to Korea in 2017. However, with disclosure requirements gradually expanding, it is anticipated that, by 2026, such requirements will become applicable to all publicly traded companies on the KOSPI market.

In addition to the above, publicly traded companies are subject to various other regulations under applicable laws and regulations, such as the requirement to include certain information about candidates for directors or auditors in the notice convening a shareholders meeting, and the requirement to make disclosures on a regular basis or in relation to transactions of a certain nature.

Key issues in corporate governance reporting will be discussed hereafter.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance ESG Disclosure Rules

The Financial Services Commission announced plans to require publicly listed companies to adopt mandatory ESG disclosure rules by 2026, and South Korea is preparing disclosure standards and timelines to align with global standards as well.

The Financial Services Commission plans to establish standards by referring to relevant standards from the EU, the US, and other jurisdictions, while taking into account the specific characteristics of the domestic market and companies. These standards will be introduced gradually, beginning with large publicly traded companies, based on the readiness of the disclosing entities. However, considering the delay in discussions on mandatory ESG disclosures in major countries such as the US, introducing ESG disclosure regulations in Korea may be further delayed.

Rise in Shareholder Activism

Shareholder activism has been on the rise in recent years, increasing ninefold since 2019 in Korea with 77 companies headquartered there targeted by activist campaigns in 2023, according to a report published by the Federation of Korean Industries. For further information on shareholder activism campaigns, please refer to the Trends & Development section (link).

2.2 ESG Considerations

For publicly traded companies, the Corporate Governance Report system aims to enhance governance transparency.

Currently, companies in the KOSPI with assets exceeding KRW1 trillion are required to submit

corporate governance reports according to the guidelines of the Korea Exchange, which are continuously revised. As per the revised guidelines in 2025, the corporate governance report must include compliance with a total of 15 key indicators for shareholders, the board of directors, and internal audit. These indicators must show:

- whether dividend predictability is ensured;
- that communication with minority shareholders and institutional investors is improved;
- the status of financing, with different shareholder interests;
- that the board is sufficiently diverse;
- that a reasonable compensation policy for directors is in place; and
- that no unqualified executives have been appointed.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies involved in the governance and management of a company in South Korea are (i) the general meeting of the shareholders, (ii) the board of directors, and (iii) the statutory auditor (or audit committee).

General Meeting of the Shareholders

The shareholders' meeting is the highest decision-making body that resolves important matters for the company. As the name implies, the members of the shareholders' meeting are shareholders, while directors and auditors may attend the meeting but are not official members.

The Board of Directors

The board of directors is a standing body organised to make key decisions on the conduct of a

company's business. Most companies have a board of directors, but for smaller companies of under a certain size, the shareholders' meeting or directors may serve in this role.

The board of directors is composed of all directors, regardless of whether they are inside directors, outside directors or non-executive directors. However, as mentioned above, in the case of a publicly traded company, the board of directors must be composed of at least a certain percentage of outside directors.

Statutory Auditor/Audit Committee

The statutory auditor has the authority to attend the board of directors' meetings and inspect and supervise directors' performance, audit the accounts and ensure general compliance with the law (similar to outside directors).

According to the KCC, joint stock companies with paid-in capital of KRW1 billion or more must appoint a statutory auditor or establish an audit committee, regardless of whether they are publicly traded companies or not, while publicly traded companies with total assets exceeding KRW2 trillion must establish an audit committee instead of simply appointing a statutory auditor.

An audit committee must consist of three or more directors, with outside directors making up two-thirds or more of its members. In the case of publicly traded companies, at least one member of the audit committee must be a financial or accounting expert, and the chairperson must be an outside director.

Representative Director

The representative director has the authority to represent the company externally and execute internal operations, and is an essential figure within a joint stock company. According to

the KCC, the representative director must be appointed by the board of directors, although the articles of incorporation may allow for appointment by the shareholders' meeting.

While many companies typically have only one representative director, it is also permitted for companies to have more than one. In the case of multiple representative directors, such representative directors may be granted (i) the authority to jointly represent the company, in which case they will act together in their executive actions, or (ii) the authority to independently represent the company, in which case each of them will, alone, act independently in their executive action.

3.2 Decisions Made by Particular Bodies General Meeting of the Shareholders

The major decisions made by the general meeting of shareholders include, without limitation, the following:

- appointment of directors and auditors;
- approval of the financial statements;
- dividend distribution; and
- amendments to the articles of incorporation and other significant corporate actions (such as M&A, corporate restructuring, dissolution and liquidation, etc).

Under the KCC, the following decisions must be reserved for the shareholders, and may be resolved by a majority of votes among the shareholders present at the general meeting representing more than a quarter of the total outstanding shares of the company:

- appointment of a director or a statutory auditor;
- approval of the annual financial statements;

- approval of remuneration of directors and statutory auditors; and
- declaration of dividends.

For the following decisions that are reserved for the shareholders, the KCC requires a special resolution achieving more than two-thirds of the votes of shareholders present at the general meeting representing more than a third of the total outstanding shares of the company:

- transfer of all or a material portion of the company's business;
- removal of directors and statutory auditors;
- amendments to the articles of incorporation of the company;
- capital reduction;
- mergers and spin-offs of the company;
- dissolution or continuance of the company; and
- granting of stock options.

The Board of Directors

The major decisions made by the board of directors relate to, without limitation, the day-to-day operation of the company (to the extent not reserved for a general meeting of shareholders).

According to the KCC, resolutions of the board of directors must be made by a majority vote of the attending directors, in the presence of the majority of directors. The main resolutions of the board of directors include:

- the convening of the meeting of shareholders;
- appointment of representative directors;
- issuance of new shares;
- disposal of significant assets;

(On the other hand, the requirements for board resolutions may further be reinforced by laws or articles of incorporation. For example, the

approval of two-thirds of the directors is required for the following under the KCC, and companies may have different (ie, higher, but in no case lower than stipulated under the applicable laws) resolution requirements in their articles of incorporation.)

- use of business opportunities of the company by directors; and
- transactions between directors and the company.

The board of directors will have decision-making authority over the execution of business and other important matters as designated by the KCC, articles of incorporation, regulations of the board of directors and resolutions passed by the board of directors. However, the representative director will have decision-making authority over the details of business execution or routine business.

3.3 Decision-Making Processes

The general meeting of the shareholders ("*Ordinary General Meeting of the Shareholders*") must be held at least once every year and at any time that is necessary giving two weeks' notice, although the notice period may be waived or shortened by the unanimous consent of the shareholders, in which case the meeting becomes the "*Extraordinary General Meeting of the Shareholders*", according to the KCC.

As specified above, pursuant to the KCC, voting at the general meeting of the shareholders generally requires majority approval (ie, a majority of votes from the shareholders present at the general meeting, representing more than a quarter of the total outstanding shares of the company), although certain matters (including amendment to the articles of incorporation or dissolution/liquidation) require special majority

approval (ie, more than two-thirds of the votes of the shareholders present at the meeting, representing more than a third of the total outstanding shares of the company). According to the KCC, only one vote is allowed per share. Additionally, proxy voting is permitted. If specified in the articles of incorporation, publicly traded companies may notify minority shareholders of the general meeting through publication in two or more daily newspapers or by electronic means.

Meeting of the Board of Directors

The meetings of the board of directors may be held regularly (as stipulated in the articles of incorporation and/or shareholders agreement/joint venture agreement, if applicable) and at any time, provided that a week's notice is given, in accordance with the KCC. The notice period may be waived or shortened by the unanimous consent of the members of the board of directors. However, unlike the shareholders' meeting, the notice period can be shortened by the articles of incorporation, with the result that many companies shorten notice to one or three days in their articles of incorporation.

As mentioned above, voting at board of directors meetings generally requires majority approval unless stipulated otherwise by the articles of incorporation and/or shareholders agreement/joint venture agreement, if applicable. Unlike shareholder meetings, the board of directors meeting does not recognise proxy voting, requiring directors to be present and vote in person.

4. Directors and Officers

4.1 Board Structure

The board of directors in South Korea usually has a one-tier structure, and typically consists of inside directors (executive directors), out-

side directors (independent directors) and non-executive director (other directors not directly engaged in the regular business of the company). One or more of the inside directors is also appointed as (a) representative director(s) of the company.

While statutory auditors are not members of the board of directors, they have the right to attend board of directors meetings. The audit committee is treated as a subcommittee established within the board of directors.

4.2 Roles of Board Members

There are three types of director: inside director, outside director and non-executive director. While specific roles are not expressly designated by the KCC, there are some differences among them. For instance, outside directors are required to have independence, and only inside directors can be appointed as the representative director. A brief instruction of each director type is as follows.

Inside Director

Inside directors are those engaged in the day-to-day management of a company.

Outside Director

Outside directors are those not directly engaged in the day-to-day management of a company but are expected to take care of the objective oversight of the day-to-day matters, including those relating to governance and general compliance. To be appointed as an outside director, one must not have any of the disqualifications specified by the KCC.

Non-Executive Director

Non-executive directors are those that are not directly engaged in the day-to-day management of a company, but are not deemed to be

outside directors. They are not required to have independence, unlike outside directors, and are treated like inside directors in terms of legal regulations.

Regardless of whether a member is an inside director, outside director or non-executive director, each (other than the statutory auditor) shall have an equal vote over any matter submitted to the board of directors for approval, and no casting vote is permitted under the KCC.

4.3 Board Composition Requirements/Recommendations

Under the KCC, a company with total capital of less than KRW1 billion may have one or two directors, otherwise the requirement is to appoint at least three directors. The size of the board of directors can also be determined in the articles of incorporation, subject to the foregoing requirements under the KCC.

For outside directors (ie, one of the members of the board of directors), a publicly traded company must appoint more than one-quarter of its directors as outside directors; a large publicly traded company with total assets of equal to or above KRW2 trillion must appoint three or more outside directors, making up the majority of the board of directors.

As stated, when establishing an audit committee within the board of directors, the committee must consist of three or more directors, with outside directors making up two-thirds or more of the members. In the case of publicly traded companies, at least one member of the audit committee must be a financial or accounting expert, and the chairperson of the audit committee must be an outside director.

4.4 Appointment and Removal of Directors/Officers

Shareholders have the power to appoint or remove directors through the general meeting of the shareholders. Under the KCC, the appointment of directors will require a majority of votes of shareholders present at the general meeting representing more than a quarter of the total outstanding shares of the company; for the removal of directors, more than two-thirds of the votes will be required from those shareholders present at meeting, representing more than a third of the total outstanding shares of the company.

Although there are no particular criteria for becoming a director, a statutory auditor of a company cannot also hold the office of director.

Furthermore, a person who falls within any of the following categories cannot be an outside director of a company:

- directors and employees engaged in the regular business of the company, or directors, auditors and employees who have been engaged in the regular business of the company within the previous two years;
- in instances where the largest shareholder is a natural person, the largest shareholder, their spouse, lineal ascendants and lineal descendants;
- in instances where the largest shareholder is a company, directors, auditors and employees of the largest shareholder;
- spouses, lineal ascendants and lineal descendants of directors, auditors or executive officers of the company;
- directors, auditors, executive officers and employees of the parent or subsidiary of the company;
- directors, auditors, executive officers and employees of another company that has a

- significant interest in the company, such as business relations with the company; and
- directors, auditors, executive officers and employees of another company in which directors or employees of the relevant company work as directors, auditors, executive officers or employees.

In addition, the KCC stipulates additional reasons for disqualification of an outside director of a publicly traded company, including the following:

- a minor or a person of incompetence or of quasi-incompetence;
- a person for whom two years have not passed since being dismissed or removed from office after they violated acts relating to finance separately determined by presidential decree, including, but not limited to, the FISCMA, the Banking Act and the Insurance Business Act;
- the largest shareholder and their specially related persons;
- a shareholder who owns more than 10% of the total number of issued shares, other than non-voting shares, by their calculation, regardless of the name of a shareholder, or who exerts de facto influence on important matters related to the management of publicly traded companies and their spouse, lineal ascendants and lineal descendants; and
- a person determined by presidential decree to have difficulty faithfully performing their duty as an outside director, or who may have an influence on the management of publicly traded companies.

4.5 Rules/Requirements Concerning Independence of Directors

Generally, the board of directors takes a holistic approach to ensuring the independence of direc-

tors and preventing potential conflicts of interest, including by considering the totality of fact and circumstances to determine whether there is any special/material relationship between a director and the affairs of the company. According to court decisions, a special/material relationship between any director and the affairs of the company exists if there is a personal conflict with the matter being discussed and decided upon (eg, if the director becomes a counter-party to a transaction with or in a matter against the company, or if the discussion and vote concern their compensation).

If it is determined that there is any special/material relationship between any director and the affairs of the company, the director will not be permitted to vote on the company's relevant affairs.

With regard to the rules and requirements around the independence of “*outside directors*,” please refer to **4.4 Appointment and Removal of Directors/Officers**.

4.6 Legal Duties of Directors/Officers

Under the KCC, a company director is considered an agent of that company with two primary categories of duty: (i) the duties of a good faith caretaker toward the company (“*Duty of Care*”) (Article 382 (2) of the KCC; Article 681 of the Civil Act); and (ii) the duties to act in good faith in the interests of the company in compliance with the relevant laws and the company's articles of incorporation (“*Duty of Loyalty*”) (Article 382-3 of the KCC). Furthermore, based on court decisions interpreting the KCC, a director is recognised as having a duty to oversee other directors' duties (“*Duty of Oversight*”). Duty of Care, Duty of Loyalty and Duty of Oversight shall hereinafter be collectively referred to as “*Fiduciary Duties*”.

Duty of Care

Directors execute the company's affairs according to the delegation relationship, thereby assuming a duty of care towards the company. Duty of care entails a standard of care that is generally and objectively expected of directors in transactions. It requires directors to actively execute their duties in the company's best interests, utilising the company's human and material resources to their fullest extent while prudently assuming risks. If a director breaches their duty of care, they may be subject to criminal prosecution in addition to liability for damages to the company.

However, based on court rulings, in assessing whether there has been a breach of the duty of care by a director, the Business Judgment Rule is applied. Under this rule, if a director exercised their duties based on business judgment, even if that judgment is later found to be incorrect and results in harm to the company, it does not constitute a breach of the duty of care so long as it was made in good faith and with reasonable attention.

Duty of Oversight

This is an obligation to monitor the conduct of other directors in order to prevent them from violating their duties. The scope of the duty required of directors varies depending on their roles. Inside directors, including representative directors, have the duty to oversee and supervise the general affairs of the company and the performance of all employees, including other directors.

On the other hand, based on case law, outside directors, not possessing executive authority and not engaging in day-to-day management, do not have the same scope of the duty as inside directors. However, they are judged to have vio-

lated their duty of oversight (i) when they knew or had reason to suspect that business execution by other directors has been illegal and ignored it, or (ii) have failed to fulfil appropriate actions to ensure that the company's compliance system is adequate and meets the necessary requirements to operate in the industry within which the company operates.

The duty of oversight for directors is gradually strengthening, leading directors to more actively fulfil their oversight responsibilities, and resulting in an increase in cases of directors joining directors' and officers' liability insurance.

The KCC also stipulates the following duties of a director:

- duty of confidentiality;
- duty of non-competition;
- duty against usurpation of corporate opportunities and assets;
- duty against self-dealing;
- duty to prepare financial statements; and
- duty to report.

4.7 Responsibility/Accountability of Directors

Although members of the board of directors are appointed by the shareholders of the company, the board of directors (and each of its members) represents, and owes legal duties such as Fiduciary Duties to, the company and the company only. That said, active discussions are in progress in South Korea regarding the recent expansion of the scope of Fiduciary Duties. Please see the Trends and Developments section for more details regarding these recent discussions.

Accordingly, directors assume various duties noted in **4.6 Legal Duties of Directors/Officers**,

which, if breached, will subject them to various liabilities, as detailed hereafter.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Civil Charges and Compensation for Damages

According to the KCC, directors who intentionally or negligently violate the articles of incorporation of the company or applicable laws, or omit to perform their duties, are jointly and severally liable for damages resulting from such acts or omissions.

Furthermore, if a director's violation of their duties as a director also constitutes a violation of applicable laws, the civil code requires adequate compensation for any damages resulting from such illegal actions. Whilst the Business Judgement Rule is considered when the court decides on any compensation for damages, if the director is considered to have violated their duties as a director in violation of the applicable laws, the Business Judgement Rule does not apply according to precedents.

Criminal Charges

If a director is found to intentionally have acquired, or caused any third party to acquire, any assets such as money or property as a result of any violation of their duties, resulting in any losses or damages to the company, the director shall be considered to have committed a breach of their Fiduciary Duties. This carries a prison sentence of 10 years or less, or a fine of KRW30 million or less.

If the value of the assets, such as money or property, acquired by the director or caused to be acquired by a third party is equal to or above KRW500 million but less than KRW5 billion, the applicable prison sentence will be three years

or more. If the value of the assets is equal to or above KRW5 billion, the applicable prison sentence will be five years or more (with up to life imprisonment).

It should be noted that a director owes their Fiduciary Duties only towards the company, and losses or damages to the company only (and not to the shareholders) will be used as a basis for determining the applicable penalties.

In cases of breach of duty by directors, breach of Fiduciary Duties is mainly at issue, but directors can also be held criminally liable for jeopardising the company's assets (Article 625 of the KCC) or for misrepresenting payments (Article 628 of the KCC).

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

A director may also be liable for damages to any third party resulting from their intentional or grossly negligent conduct.

Liability of a director can be limited, as follows:

- **Indemnification:** under the KCC, a company may indemnify a director by unanimous approval of the shareholders; or in accordance with its articles of incorporation, a company may indemnify an amount of liability incurred by a director that exceeds up to six times (or three times for outside directors) their remuneration for the year; however, this shall not apply in respect of loss or damage caused by the wilful misconduct or gross negligence of a director.
- **Exemption:** liability of a director may be exempted by the unanimous approval of the shareholders.
- **D&O liability insurance:** Directors' and officers' liability insurance is permitted under the

KCC. Listed companies and large Korean companies are increasingly adopting such policies into their corporate governance framework. It is common practice for Korean companies to bear the cost of the premiums of such policies.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Unless provided otherwise in the articles of incorporation, director remuneration is determined by the shareholders at the shareholders' general meeting. In practice, shareholders typically set the aggregate amount of funds available for remunerating the board of directors and then authorise the board of directors to determine between themselves the individual remuneration payable to each director. Companies that are required to submit annual reports (as described in **6.1 Financial Reporting**) must include in such reports the amount of remuneration approved at the general meeting of the shareholders and the amount of remuneration paid to all directors and statutory auditors.

Failure to comply with the requirements may result in (i) legal challenges by the shareholders, which may result in potential liabilities for directors; (ii) restitution by the member of the board of directors having received such remuneration; and/or (iii) unfavourable tax implications (ie, treatment of the company's expenses as non-deductible expenses).

4.11 Disclosure of Payments to Directors/Officers

According to the FISCMA, publicly traded companies must disclose payment to registered directors and officers with an annual salary of KRW500 million or more, as well as specific cri-

teria and methodology for calculating such payment.

Apart from the requirement for publicly traded companies to disclose the remuneration of executive officers exceeding KRW500 million, there is no specific disclosure obligation required, and private companies are not obliged to disclose the remuneration of directors and officers.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The board of directors is empowered to execute the business of the company in accordance with the KCC. Accordingly, apart from their ability to appoint or remove directors and their voting rights in shareholders' meetings, shareholders do not otherwise possess any power to require the board of directors to pursue a particular course of action.

With that said, please refer to **3.2 Decisions Made by Particular Bodies** for matters that are subject to shareholder approval.

Furthermore, please note that controlling shareholders do not owe duties to the company or to non-controlling shareholders under the KCC. It is provided, however, that any person, including a controlling shareholder, who instructs a director to conduct business by using their influence over the company, conduct business under the name of a director, or conduct business by using a title that may give the impression that they are authorised to conduct the business of the company will, in each instance, be seen as a director for the purposes of the KCC, thereby attracting liability and responsibility as a de facto direc-

tor for compensating losses resulting from such actions.

Under the KCC, a shareholder's liability is limited to the acquisition or subscription price of their shares; however, the Supreme Court of Korea has held that there may be exceptions for situations where companies are essentially sole proprietorships or deemed to have no substance, but incorporated merely for the purpose of shielding legal implications that would otherwise apply against the individual proprietor, leading to a ruling that, in such cases, the corporate veil may be pierced – thereby imposing personal liability on the individual proprietor. In addition, under Korean tax law, a shareholder who owns more than 50 per cent of the total outstanding shares of a company may, in certain cases, be liable for the company's secondary tax liability in proportion to their ownership interest.

5.2 Role of Shareholders in Company Management

In short, other than by voting on the matters reserved for shareholders, the shareholders are not permitted to direct the management of a company. However, they are able to influence the management of a company through appointment and/or dismissal of directors or by exercising their statutory rights to influence the management of a company.

Key statutory shareholder rights include the right to demand a shareholders' meeting, the right to demand the dismissal of directors/auditors, the right to inspect accounting books, and the right to maintain legal action against unlawful acts of directors/auditors.

In particular, the right to demand the dismissal of directors/auditors or to maintain legal action

against unlawful acts allows shareholders to influence the management of the company.

Shareholders exercise these minority shareholder rights and may seek a court injunction to suspend the directors' performance of their duties.

5.3 Shareholder Meetings

Under the KCC, a company is required to convene an Ordinary General Meeting of the Shareholders annually. While the KCC does not specifically stipulate the timing for holding the Ordinary General Meeting of the Shareholders, in practice, the majority of companies hold the meeting within three months of the end of the preceding fiscal year.

In addition to the Ordinary General Meeting of the Shareholders, the Extraordinary General Meeting of the Shareholders may be held from the time to time as necessary.

Please refer to 3.2 Decisions Made by Particular Bodies and 3.3 Decision-Making Processes for the procedures and resolutions related to the general meeting of the shareholders.

5.4 Shareholder Claims Claims Against Directors

For claims against directors discussed in 4.8 Consequences and Enforcement of Breach of Directors' Duties, shareholders of a company are also considered third parties that can claim compensation for damages from directors due to negligence in their duty to act. However, court decisions have only allowed for compensation claims for damages where the shareholder directly incurs damages from the director's negligence, and not in situations in which the company is the one to incur damages, which then affects the shareholder negatively (indirect damages).

Derivative Actions

With respect to any indirect damages (through damages incurred by the company), the shareholders may bring a derivative action against the directors on behalf of the company.

Specifically, if a director causes damage to the company through violation of laws or articles of incorporation, or through negligence in performing their duties, the shareholders can demand that the company file a lawsuit to hold the director accountable. If the company does not file a lawsuit against the director within 30 days of receiving such a demand, the shareholders can immediately file a lawsuit against the director on behalf of the company to claim damages as derivative actions (Article 403 of the KCC).

In the case of private companies, shareholders owning more than 1% of the total issued shares can file such lawsuits. However, for publicly traded companies, only the shareholders who have continuously held at least 0.01% of the total issued shares for the past six months can initiate representative lawsuits (Article 542-6, Paragraph 6 of the KCC).

5.5 Disclosure by Shareholders in Publicly Traded Companies

The 5% Reporting Rule

Any individual or entity holding 5% or more of a publicly traded company's total outstanding shares must report their share-ownership status, changes in holdings, and the purpose of their holding to the Financial Services Commission. The 5% threshold for disclosure is calculated by aggregating not only the shares held by the relevant shareholder but also the shares held by such shareholder's related parties. In this case, the individual holding the largest number of shares (when aggregated with the shares held by their related parties) has the right to file the

report as the representative reporter, enabling consolidated reporting.

The 10% Reporting Rule

An individual ("*major shareholder*") who acquires ownership of 10% or more of the total issued shares of a company is required to disclose this ownership, and any subsequent changes in the number of shares owned must also be disclosed. However, if the change in the shareholding involves less than 1,000 shares and the applicable amount is lower than KRW10 million, the obligation to report the change does not apply. Unlike the 5% rule, the 10% rule does not aggregate the number of shares held by related parties.

There is no disclosure obligation in relation to the ultimate beneficial owner of publicly traded companies, although such disclosure may be required in certain regulated industries (eg, financial institutions).

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Listed and certain other companies are obliged to submit an annual report, and regular disclosures must be made on its business through quarterly, semi-annual and annual reports, which are made available to the public on an electronic public disclosure platform maintained by the Financial Supervisory Service such as the "*Data Analysis, Retrieval and Transfer System*" (DART).

In addition, such companies must submit timely reports setting forth information on material events having an effect on the management or assets of the company (eg, mergers, spin-offs, comprehensive exchanges of shares, transfers

of a material business (assets), sales or transfers of treasury stock and issuance of convertible bonds or bonds with warrants). Such reports are also made available to the public on DART.

“Certain other companies” include those that (pursuant to the External Audit Act and FISCMA) intend to be publicly traded in the relevant or subsequent fiscal year and meet the following conditions:

- have total assets of KRW50 billion or more as at the end of the preceding fiscal year or total revenue of KRW50 billion or more for the preceding fiscal year.
- fulfil any two of the conditions below:
 - (a) have total assets of KRW12 billion or more as at the end of the preceding fiscal year;
 - (b) have total liabilities of KRW7 billion or more as at the end of the preceding fiscal year;
 - (c) have total revenue of KRW10 billion or more for the preceding fiscal year; or
 - (d) have a total headcount of 100 or more as at the end of the preceding fiscal year.

6.2 Disclosure of Corporate Governance Arrangements

For private companies, the articles of incorporation must be kept at the head office and are not made publicly available, although certain parts of the articles (such as the business objectives of the company and the terms of the preferred shares and convertible or redeemable securities) may be gathered from the commercial registry maintained with the court registrar. Any shareholders or creditors of a company may, at any time during its business hours, inspect the articles of incorporation and request a copy thereof.

For publicly traded companies, the articles of incorporation are attached to the annual report and are publicly available on DART.

Furthermore, under the FISCMA, companies that are required to submit annual reports, such as publicly traded companies, must submit quarterly, semi-annual and annual reports to the Financial Services Commission and to the Korea Exchange, which are then publicly disclosed. These reports contain information relating to the composition of the board of directors, major items resolved by the board of directors, including whether each outside director voted in favour of or against such items and, if applicable, the composition and activities of the subcommittees of the board of directors.

6.3 Companies Registry Filings

Certain key information relating to a company, including the registration number, name, registered address, method of public notification, capitalisation, business purposes, information on directors and statutory auditor and information on rights of class shares, among other information, is required to be registered with the court registrar.

Failure to comply with this requirement may result in penalties or other sanctions (eg, fines). Companies that consistently fail to comply with this requirement may also lose their good standing and, in extreme cases, be subject to administrative dissolution.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Listed companies and certain other companies (as described in 6.1 Financial Reporting) must

appoint an external auditor for its financial statements.

Pursuant to the External Audit Act, individuals with a vested interest in the company cannot serve as auditors, ensuring that external auditors can perform their duties independently in a separate/independent capacity.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

There is no specific and express legal requirement for directors with regard to the management of risk and internal controls in a company, although they are expected (within the scope of their Fiduciary Duties) to assess and manage risks, oversee internal controls and monitor general compliance.

Specifically, the responsibilities that directors bear as trustees with respect to internal controls can include Fiduciary Duties, including their oversight duty described in 4.6. **Legal Duties of Directors/Officers**. If directors breaches these duties, they may be held liable for civil damages and subject to criminal penalties.

Trends and Developments

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Lee & Ko

Lee & Ko has an M&A team of approximately 150 attorneys. The firm provides comprehensive legal services for various types of M&A transactions, including those involving financial institutions, privatisations of public corporations, tender offers, corporate mergers/spin-offs and restructuring through the conversion of holding companies. The team works across many industries, including finance, energy, chemicals, food, medical, broadcasting, technology, enter-

tainment and start-ups. By collaborating with other practice groups such as tax, labour, anti-competition and regulatory compliance, Lee & Ko provides clients with a seamless, one-stop service throughout the entire M&A process. The firm's offices in Beijing, Ho Chi Minh City and Hanoi also provide M&A-related legal services. The M&A team has handled significant deals across all industry sectors both domestically and internationally.

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SOUTH KOREA TRENDS AND DEVELOPMENTS

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Legislative Developments to Revitalise Capital Market and Enhance Regulatory Oversight

In Korea, amid a surge in retail investor participation in the stock market, addressing the so-called “Korea Discount” where the stock prices of Korean listed companies are undervalued compared to those in other countries with similar net asset values and profitability – has emerged as a major policy challenge. While low shareholder returns, structural issues in domestic industries, and stringent foreign exchange regulations are all considered as factors contributing to the Korea Discount, from a legal perspective, the lack of effective legal mechanisms to restrict controlling shareholders’ pursuit of their own private interests over interests of all shareholders has been identified as a key reason why corporate profits are not fairly distributed to minority shareholders in Korea.

To resolve the Korea Discount issue and better protect minority shareholders, the Korean government undertook various reforms to the capital market regulations in 2024 by amending the Enforcement Decree and other subordinate regulations of the Financial Investment Services and Capital Markets Act (FSCMA) applicable to listed companies. In addition, more fundamental legislative changes, such as amendments to the Korean Commercial Code (KCC), are being discussed to address the inherent conflicts of interest between controlling and minority shareholders.

Amendments to Enforcement Decree of FSCMA in 2024

Granting Autonomy in Calculation of Merger Prices for Listed Companies

Under the pre-amendment Enforcement Decree of the FSCMA, merger ratios for listed companies were determined based on a legally pre-

scribed formula which took into account stock prices as of the date of the board resolution approving a merger, and only limited adjustments within a fixed range were allowed. There have been ongoing concerns that the foregoing approach could hinder structural improvements based on determination of a merger ratio as agreed between private parties, and that it could be exploited by controlling shareholders to conduct mergers at a specific time (ie, when the stock price of a company with a higher ownership percentage is favourable for the controlling shareholder), thereby resulting in mergers that benefit those controlling shareholders.

Effective from 26 November 2024, the amended Enforcement Decree of the FSCMA abolished the statutory formula for calculating merger prices in principle, thereby enabling parties to determine merger terms through negotiation. However, for mergers between affiliates or involving special purpose acquisition companies (SPACs), the previous rule still applies. In such cases, the base price is calculated as the weighted average of: (i) the one-month average closing price; (ii) the one-week average closing price; and (iii) the most recent closing price, with a permitted adjustment range of 10% for affiliate mergers and 30% for SPAC mergers.

Enhancing Disclosure and Independent Evaluation Requirements for Mergers

The amended Enforcement Decree of the FSCMA aims to enhance procedural fairness and transparency in mergers by moving away from the regulation of valuation of merging companies through statutory formula and introducing robust disclosure and independent evaluation requirements for valuation.

- Previously, minority shareholders lacked access to board-level discussions on merg-

ers, making it difficult to challenge decisions that favoured controlling shareholders. The amended FSCMA now mandates that the board of a listed company is required to prepare and publicly disclose a written statement including: i) the purpose and anticipated effects of the merger; ii) the appropriateness of the merger price; iii) the fairness of transaction terms such as merger ratio; and iv) any dissenting opinions from board members and reasons for such dissent, with their signatures. Through the newly required mandatory preparation and disclosure of the statement, minority shareholders are now able to make investment decisions based on more meaningful information regarding mergers. From the company's perspective, the amended rule has increased the need to engage in more proactive explanation and justification of the rationale for the merger and the appropriateness of the merger ratio to minority shareholders.

- Under the amended Enforcement Decree of the FSCMA, an external evaluation of the merger price is required for both mergers between affiliated companies and those between unaffiliated companies. In addition, the procedures and requirements for selecting external evaluation agency have become more stringent: companies are now required to obtain the consent of statutory auditor or the approval of audit committee when selecting an external evaluation agency; disqualifying criteria for external evaluation agency have been strengthened; and external evaluation agencies are now required to comply with newly established quality management standards when performing merger-related evaluations.
- The mandatory disclosure of board opinions and third-party valuation requirements described above apply not only to mergers

but also to material business/asset transfers, material asset transfers, and comprehensive share exchanges/transfers.

Regulations on Treasury Stocks of Listed Companies

Pursuant to the amended Enforcement Decree of FSCMA effective as of 31 December 2024, the following regulatory changes were made with respect to the acquisition and disposal of treasury stocks by listed companies.

- While treasury stocks are generally deprived of shareholder rights such as voting right and right to receive dividends, the statutory provisions and court precedents have been unclear as to the right to receive newly issued shares during corporate mergers and spin-offs. As such, in practice, newly issued shares were frequently allocated to treasury stocks during mergers and spin-offs. In particular, during a spin-off, when new shares of the company newly established through spin-off ("*Spin-Off Company*") are allocated to treasury stocks held by the original company ("*Original Company*") subject to such spin-off, the controlling shareholder of the Original Company may, in addition to new shares received in proportion to its shareholding ratio in the Original Company, also indirectly gain additional control over the Spin-Off Company through the shares allocated to treasury stocks. This so-called "*magic of treasury stocks*" effect has been criticised as a means by which controlling shareholders strengthen their control through spin-offs. Under the amended FSCMA, where a listed company intends to conduct a spin-off or a spin-off merger, the Spin-Off Company is prohibited from allocating new shares to treasury stocks held by the Original Company, and the Original Company is not allowed to transfer

its treasury stocks to the Spin-Off Company. Furthermore, in the case of a merger involving a listed company, the surviving company is prohibited from allocating new shares to the shares of the non-surviving company held by the surviving company, or to the treasury stocks held by the non-surviving company. The transfer of treasury stocks in such instances from the surviving company to the non-surviving company is also prohibited. These amendments are expected to prevent abuse of merger and spin-off mechanisms by controlling shareholders to strengthen their control.

- In addition, under the amended Enforcement Decree of the FSCMA, disclosure obligations have been strengthened with respect to the acquisition and disposal of treasury stocks. The regulatory framework has also been revised to address and eliminate regulatory deficiencies associated with acquiring or disposing of treasury stocks via trust, which were subject to less stringent regulations compared to direct acquisitions of treasury stocks.

Prior Disclosure Requirement for Insider Transaction of Listed Companies

Effective 24 July 2024, executives (including directors) and major shareholders (holding 10% or more) of listed companies are now required under the amended FSCMA to disclose planned transactions involving certain securities (eg, equity securities, convertible bonds, bonds with warrants, and related depositary receipts) of their companies at least 30 days prior to expected trading date.

Previously, the FSCMA only required post-transaction disclosure by major shareholders and executives upon disposal of securities. The revised regime aims to enhance transparency

in insider transactions and ensure fairness for general investors.

- *Scope of insiders* – includes not only directors and officers but also de facto executives (including anyone with substantial influence over key managerial matters including the appointment and dismissal of executives), but excludes financial investors, such as certain investment vehicles and special purpose companies.
- *Scope of transactions* – the transaction must be disclosed if it involves the purchase, sale, or other disposition of shares or other relevant securities issued by a listed company. However, the disclosure requirement is exempted if both of the following conditions are met: i) the aggregate number of shares (or relevant securities) traded over the past six months (based on the transaction commencement date) and during the transaction period is less than 1% of the total number of the issued and outstanding shares of the listed company; and ii) the aggregate transaction amount is lower than KRW5 billion. In addition, transactions conducted pursuant to the applicable laws and regulations (eg, statutory acquisitions or sales), M&A transactions conducted by transfer of shares, and acquisitions or disposals resulting from mergers or spin-offs are also exempt from the disclosure requirement.
- *Procedures* the transaction plan, including details such as purchase price, number of shares and transaction period, must be reported at least 30 days prior to the transaction commencement date. The transaction must be completed within 30 days from the scheduled commencement date, and deviations from the submitted transaction plan are permitted only within 30% range of the previously planned transaction amount.

- *Penalties* in the event of a violation (eg, failure to disclose the transaction plan, false disclosure, or failure to execute the disclosed transaction plan) an amount corresponding to 0.02% of the market capitalisation can be imposed as a penalty surcharge, which is capped at KRW2 billion.

Potential Future Legislative Amendments

Thus far, so-called “*targeted regulations*” have been introduced under the FSCMA to address specific areas such as merger procedures, restrictions on the acquisition and disposal of treasury stock, and disclosure obligations. However, legislative discussions are also underway to more comprehensively and fundamentally resolve the conflict-of-interest issue between the controlling shareholder and minority shareholders. Among these, the two most actively discussed and potentially impactful reforms – which, if adopted, are expected to bring significant changes to capital markets and related practices – are: i) amendments to the KCC to expand the scope of directors’ duty of loyalty; and ii) the introduction of a mandatory tender offer regime.

Expansion of Directors’ Duty of Loyalty Scope

A proposed amendment to the KCC that imposes a duty of loyalty on directors toward shareholders passed the plenary session of the National Assembly on 13 March 2025. However, the legislative process was suspended when the Acting President exercised the right to request reconsideration (ie, veto on legislation) on 1 April 2025. The National Assembly attempted to re-pass the bill on 17 April 2025, but the bill did not pass and was subsequently abandoned.

Despite strong criticism from the business community, public opinion continues to support the

necessity of amending the KCC to fundamentally address the issue of controlling shareholders’ pursuit of private interests and the resulting harm to minority shareholders. Given that the majority party in the National Assembly has taken a highly supportive stance on the proposed amendment, there remains a significant possibility that the bill will be reintroduced and passed in the near future.

The proposed amendment to the KCC provides that “*a director shall faithfully perform his or her duties for the benefit of the company and its shareholders in accordance with applicable laws and the articles of incorporation*”, thereby expanding the scope of a director’s duty of loyalty to include not only the company but also its shareholders. Furthermore, the amendment stipulates that directors must protect the interests of all shareholders and treat them equitably in the performance of their duties.

If this amendment is ultimately enacted, companies will be expected to conduct a more thorough review from the perspective of shareholder protection when undertaking corporate restructurings or capital transactions, such as mergers or divestments. While it is generally understood that the interests of a company align with those of its shareholders, and that a director’s duty of care and loyalty as an agent of the company inherently includes the protection of shareholder interests, the current interpretation of the KCC could already be viewed as embedding such an obligation for the directors. However, in corporate restructuring or capital transactions where minority shareholders in Korea have raised concerns about the infringement of their proportional interests – such as the listing of a spun-off subsidiary, allegations of unfair merger ratios, or third-party allotments of new shares – the proposed amendment may lead to an interpretation

requiring clearer justification that such transactions serve not only the interests of the controlling shareholder but also those of the entire shareholder base.

Mandatory Tender Offer Regime

On 21 December 2022, the Financial Services Commission (FSC) announced its plan to introduce a mandatory tender offer regime aimed at enhancing the rights of minority shareholders in cases of change of control through transfer of shares. In 2023, several bills – including the proposed amendment to the FSCMA reflecting this regime – were introduced at the National Assembly.

Under the FSC's proposal, a person intending to acquire 25% or more of a listed company's shares and thereby becoming a controlling shareholder would be required to purchase an additional *"50% plus one share"* through a mandatory tender offer with minority shareholders at the same price paid for such controlling stake. Meanwhile, some legislative proposals submitted by members of the National Assembly go further, calling for the acquirer to purchase 100% of the remaining shares through the tender offer.

While it is difficult to predict the details of the mandatory tender offer regime to be introduced and the timing of adoption, the public opinion highly supports the introduction efforts. Further, there are already numerous analyses in academia relating to the adoption of the mandatory tender offer regime as well. Therefore, it appears likely that the regime itself will be adopted at some point, but the details of the regime to be actually adopted are still unclear.

Considering the current status of the Korean M&A market, where most transactions are conducted as some form of share transfer, the introduction of the mandatory tender offer regime will bring material changes to M&A practice in Korea. For purchasers, the cost of M&A transactions will increase substantially, since they would be required to secure the majority of the target shares. For sellers, engaging in M&A will be less appealing, as they will be splitting the premiums attached to controlling stakes with other minority shareholders. At the same time, the mandatory tender offer will afford certain companies a defensive stance in hostile takeover attempts. It will therefore be important to closely follow details of the regime to be adopted, including price and threshold of shares, and to plan any potential M&A deals with consideration towards timing.

SWITZERLAND



Law and Practice

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Schellenberg Wittmer

1. Introductory

1.1 Forms of Corporate/Business Organisations

The principal forms of corporate organisations in Switzerland are the stock corporation (*Aktiengesellschaft* (AG)) and the limited liability company (*Gesellschaft mit beschränkter Haftung* (GmbH) or LLC). The stock corporation is the most important company form; it is suitable for all sizes and types of business and is the only company form that can be listed on a stock exchange. Both the AG and LLC feature a separate legal personality, a predetermined capital divided into shares or quotas and a limitation of liability to their own assets.

1.2 Sources of Corporate Governance Requirements

Primary Sources

The primary sources of law relating to corporate governance are the Swiss Federal Code of Obligations (CO) (namely the Swiss company law in Article 620 et seq. CO) and, for listed corporations, the Swiss Federal Act on Financial Market Infrastructure and Market Conduct in Securities and Derivatives Trading (the “*Financial Market Infrastructure Act*” or FinMIA).

Swiss Company Law

Swiss company law has undergone a comprehensive revision, which came into force on 1 January 2023 (for an overview of various relevant new provisions, see 2.1 Hot Topics in Corporate Governance).

FinMIA

The FinMIA regulates the organisation and operation of financial market infrastructure and the conduct of financial market participants in securities and derivatives trading.

The FinMIA is further specified by three ordinances on stock exchanges and securities trading:

- the Financial Market Infrastructure Ordinance (FinMIO) is issued by the Swiss government (Federal Council) directly;
- the FINMA Financial Market Infrastructure Ordinance (FinMIO-FINMA) is issued by the Swiss Financial Market Supervisory Authority (FINMA); and
- the Takeover Ordinance (TOO) regulating public takeovers is issued by the Swiss Takeover Board (TOB).

In addition to the issuance of ordinances in its field of competence, the regulatory body FINMA

also has the authority to issue directives (circulars). The following are relevant:

- the FINMA circular “*Remuneration schedules*” (2010/01, as amended 4 November 2020), addressing the minimum standards for remuneration schemes of financial institutions; and
- the circulars “*Corporate Governance – insurers*” (2017/02, of 1 January 2017) and “*Corporate Governance – banks*” (2017/01, as amended 4 November 2020), both addressing corporate governance, risk management and the internal control system at insurance companies and banking institutions, respectively.

Listing Rules

The two Swiss stock exchanges, SIX Swiss Exchange AG (SIX) and the smaller BX Swiss AG (BX), both self-regulatory organisations under the FinMIA, have issued listing rules with specific reporting and disclosure requirements, partially amended by the new Financial Services Act (FinSA) as of 1 August 2021. Further, to improve transparency on corporate governance, SIX Exchange Regulation, the regulatory division of SIX, has enacted the “*Directive on Information Relating to Corporate Governance*” (“*SIX Directive Corporate Governance*”), as last amended on 1 January 2023. It requires issuers with a main Swiss listing to disclose, in a separate chapter of their annual report, important information on the management and control mechanisms at the highest corporate level, or to give valid reasons for not doing so (“*comply or explain*”).

In addition, the SIX “*Directive on the Disclosure of Management Transactions*”, as amended on 1 February 2024, requires issuers with a main Swiss listing and (indirectly) their members of the board of directors and of the executive management, to disclose and report transactions of the members of the board of directors and of

the executive management in their respective securities.

Furthermore, the revised Swiss company law provides for a statutory say-on-pay regime applicable to the remuneration of the members of the board of directors, executive management and advisory board (if any) of public Swiss companies – ie, stock corporations incorporated under Swiss company law whose shares are listed, either on a stock exchange in Switzerland or abroad. The statutory provisions do not apply, in particular, to Swiss companies that have solely listed debt securities or non-voting participation certificates outstanding, and, in general, not to any privately held companies.

Corporate Governance Standards

The Swiss Code of Best Practice for Corporate Governance, as amended on 6 February 2023 (SCBP), issued by *economiesuisse*, Switzerland’s leading business association, following the entry into force of the revised Swiss company law, establishes corporate governance standards in the form of non-binding recommendations (“*comply or explain*”). The SCBP primarily addresses Swiss public companies, but also serves as a guideline for non-listed Swiss companies and organisations of economic significance. Being an effective instrument of self-regulation, it structures, integrates and reflects various Swiss law provisions on corporate governance and accepted corporate practice and sets corporate governance standards. While classified as soft law, the SCBP is widely recognised and observed by many companies in Switzerland (see 2.1 Hot Topics in Corporate Governance).

Guidelines for Institutional Investors

An important group of representatives of Swiss institutional investors (such as the Swiss Asso-

ciation of Pension Fund Providers and the Federal Social Security Funds), Swiss businesses (including the Swiss Business Federation *economiesuisse*) and proxy advisers (Ethos) have issued the “*Guidelines for institutional investors governing the exercising of participation rights in public limited companies*”. Unlike the SCBP, which primarily targets listed companies, these non-binding guidelines are directed at institutional investors. They aim at strengthening good corporate governance by outlining best practices for exercising participation rights in Swiss-listed companies. The Guidelines’ importance increased when Swiss pension funds became legally required to exercise their voting rights and disclose their voting decisions (today in accordance with the Federal Act on Occupational Old Age, Survivors’ and Invalidity Pension Provision (OPA)).

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Companies with publicly traded shares have to comply with additional corporate governance requirements. In particular, the election and remuneration of the board of directors is more strictly regulated. The chairperson, as well as each member of the board of directors, the members of the compensation committee, and the independent proxy, have to be appointed individually and annually by the shareholders’ meeting.

The board’s proposal on the compensation for the board of directors and for the executive management (and, if any, of an advisory board) has to be submitted annually to the shareholders for a binding vote (binding say-on-pay).

Additionally, the Listing Rules of the SIX and BX establish specific reporting and disclo-

sure requirements and, finally, the SIX Directive Corporate Governance requires SIX-listed companies to disclose key information on the management and control mechanisms at the highest corporate level in their annual business reports – or provide valid reasons for not doing so (“*comply or explain*”).

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In 2024, the adaptation to the revised Swiss company law, which came into force on 1 January 2023, and the implementation of the new features of the new law into Swiss companies’ articles of association remained an important topic.

As a reminder, the revised Swiss company law introduced several key changes and governance features, such as the possibility of holding virtual and hybrid shareholder meetings (see **5.3 Shareholder Meetings**) or the introduction of a capital band. Also, the existing mandatory say-on-pay regime for listed companies was transformed into statutory company law.

Another hot topic in 2024 was the first reporting period pursuant to the new ESG/non-financial reporting and due diligence duties introduced in the CO (discussed in **2.2 ESG Considerations**). While these rules were implemented in alignment with EU regulations, the European Union itself has further developed its respective regulatory framework by adopting the Corporate Sustainability Reporting Directive (CSRD) and the Corporate Sustainability Due Diligence Directive (CSDDD). In general, the Swiss rules are currently less strict and less far-reaching than the rules in the CSRD and CSDDD. The Swiss government has started its consideration on aligning

future ESG regulation with the new EU regulation. However, very recently, both in the EU and in Switzerland, the further development of the respective rules has slowed down significantly. The European Commission has adopted new proposals, so-called Omnibus packages, that intend to simplify EU rules for citizens and business. The measures shall focus the sustainability reporting obligations on the largest companies and shall make sure they do not burden smaller companies.

Lastly, in 2024, the European Court of Human Rights (ECtHR) issued a landmark judgment in *Verein Klimaseniorinnen Schweiz and Others v Switzerland*, which requests Switzerland to adopt more effective climate measures and meet its reduction targets. Whether, however, this decision will have a palpable impact on Swiss legislation is not seen as very probable.

2.2 ESG Considerations

According to the Swiss Corporate Social Responsibility Action Plan, the Swiss government's approach focuses on:

- sensitising domestic companies to ESG;
- offering support to companies seeking to address relevant issues;
- promoting transparency; and
- establishing a best practice based on international standards.

At the same time, recent ESG-related legislative changes have been introduced, aligning with international legislative developments.

Gender Representation on the Board of Directors and in the Executive Management

Swiss-listed companies exceeding two of the following thresholds in two consecutive financial years – a balance sheet total of CHF20 million,

sales revenue of CHF40 million, and/or 250 full-time positions on annual average – are required to implement certain gender quotas for the board of directors (at least 30% of each gender) and the executive management (at least 20% of each gender) under “*comply or explain*” concept (Article 734f CO).

The threshold is calculated at group level. Any company that fails to meet the mentioned requirements must disclose the reasons for missing the quotas in its remuneration report, along with the actions that are being taken to improve the situation. Privately held stock corporations may voluntarily adhere to the gender quotas (opt-in). The quotas are subject to multi-year conformance periods (2026 for boards of directors and 2031 for executive managements) but in practice significant changes in the composition of boards and senior managements are already underway.

Disclosure Obligations Relating to Raw Material Companies

The provisions regarding transparency for raw material companies have been in force since 1 January 2021, and require major companies (ie, those which have to undergo an ordinary audit by law) to issue an annual report on payments made to state bodies, provided they are engaged, either directly or through a controlled entity, in the extraction of minerals, oil or natural gas, or in the harvesting of timber in primary forests (Articles 964d–964i CO).

Non-Financial Reporting Obligations

As of 1 January 2022, the Swiss Parliament implemented new rules regarding “*transparency on non-financial matters*” encompassing new respective reporting obligations for non-financial matters (Articles 964a–964c CO).

The reporting obligations apply to Swiss “*companies of public interest*” ie, Swiss-listed companies and certain FINMA-supervised financial institutions – if they meet certain thresholds on annual average in two successive financial years:

- regarding the number of employees (at least 500 FTE); and
- with either a balance sheet total exceeding CHF20 million or revenues exceeding CHF40 million.

If within scope, the respective companies have to report on the risks of their business activities in the areas of the environment (in particular, CO₂ targets), social concerns, labour concerns, human rights and the fight against corruption, as well as on the measures taken against these risks. Violations of these reporting duties are punishable by criminal sanctions (fines). The rules are largely based on known international provisions, such as Directive 2014/95/EU (the “*Non-Financial Reporting Directive*”) concerning non-financial reporting.

The first report for non-financial matters was required to be published in 2024 for the financial year 2023.

In this context, and in light of the EU’s revised Corporate Sustainability Reporting Directive (CSRD) (Directive (EU) 2022/2464), the Swiss Federal Council has identified a need to adapt the recently introduced Swiss regulation. As a result, the Federal Council opened the consultation on new provisions regarding corporate sustainability reporting obligations. Based on the developments in the EU, this revision project has meanwhile slowed down (see **2.1 Hot Topics in Corporate Governance**).

In order to further specify the environmental aspects of the reporting obligations on non-financial matters, on 23 November 2023, the Swiss Federal Council adopted the Implementing Ordinance on Climate Disclosures, which entered into force on 1 January 2024. The Ordinance provides for the mandatory implementation of the internationally recognised recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Qualifying Swiss companies must report on:

- the financial risk that a company incurs through climate-related activities; and
- the impact of the company’s business activities on the climate and the environment.

This so-called double materiality perspective also corresponds to the approach of the EU.

Due Diligence and Disclosure Obligations Regarding Minerals and Metals from Conflict-Affected Areas and Child Labour Companies whose registered office, head office or principal place of business is in Switzerland and whose business involves so-called conflict minerals or that offer products/services that are prone to child labour must further comply with special and far-reaching due diligence and reporting obligations (Articles 964j–964l CO). In particular, the due diligence and reporting obligations in the supply chain arise if a company:

- imports minerals or specific metals containing tin, tantalum, tungsten or gold from conflict-affected and high-risk areas into or processes them in Switzerland; or
- offers products and services in relation to which there is a reasonable suspicion that they have been manufactured or provided using child labour.

In these cases, companies are obliged to set up an adequate management system and stipulate their supply chain policy and a system by which the supply chain can be traced, in order to identify and assess the risks of harmful impacts in their supply chain. In addition, these companies must draw up a risk management plan and take measures to minimise the risks identified. The report on the company's compliance with the due diligence obligations must be approved and signed by the board of directors. The board of directors must ensure that the report is published electronically immediately after approval and remains publicly available for at least ten years.

The Federal Council has additionally issued an Implementing Ordinance on Due Diligence and Transparency for Minerals and Metals from Conflict-affected Areas and Child Labour (DDTrO), which also entered into force on 1 January 2022.

Reporting Obligations on Wage Inequality

In July 2020, the Federal Act on Gender Equality was modified to include reporting obligations on wage inequality. In broad terms, companies with 100 or more employees will be required to complete an equal-pay analysis every four years. The analysis must be audited by an independent, approved third party. The results of the analysis must be shared with the workforce and, if the company is listed, with its shareholders (in the appendix to the annual report).

Private Sector ESG Disclosure Directives and Initiatives

There are several initiatives from the private sector, such as from the Swiss Bankers Association, which has declared sustainable finance as one of its strategic priorities. Among other things, this led to the development of guidelines for the advisory process for private clients. In addition,

certain Swiss proxy advisors have developed corporate governance and responsibility guidelines in connection with their voting guidelines.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

In a Swiss stock corporation, three bodies are involved in the governance and management:

- the shareholders' meeting;
- the board of directors; and
- the statutory auditors.

Shareholders' Meeting

The shareholders' meeting is the supreme body. It decides the fundamental organisation of the company, elects the board of directors and takes the fundamental decisions.

Board of Directors

The board of directors is the executive body. Swiss company law provides that the board may pass resolutions on all matters not reserved by law or the articles of association to the shareholders' meeting and shall manage the business of the company to the extent it has not delegated such management to individual members or to an executive management in accordance with organisational regulations.

Statutory Auditors

The statutory auditor is a controlling body, elected by the shareholders' meeting. However, in small companies with less than ten full-time employees, shareholders may unanimously decide not to appoint an auditor. The scope of an auditor's duties depends on the nature and size of the enterprise; listed, large and mid-sized corporations are subject to an ordinary audit,

while smaller corporations may be subject to a more limited financial audit only.

3.2 Decisions Made by Particular Bodies Shareholders' Meeting

The shareholders' meeting defines the framework of the company's business activities. In doing so, the shareholders' meeting has to decide upon the following matters, as they are fundamental, non-transferable competences attributed to the shareholders' meeting by law:

- adoption and amendment of the articles of association, including changes in the share capital, issuance of preferred shares, approval of mergers and changes in the company's corporate structure;
- approval or rejection of the annual business report, including the consolidated financial statements;
- approval or rejection of the use of the balance sheet profit and, in particular, the declaration of dividends;
- election of the members of the board of directors;
- removal of the members of the board;
- election of the external auditors;
- release of the members of the board of directors from liability (discharge);
- passing of the resolution on repaying the statutory capital reserve;
- liquidation of the company; and
- all other matters that are by law or by the articles of association reserved to the shareholders' meeting (special audit pursuant to shareholders' information rights, etc).

For listed companies, the following additional non-transferable competences are attributed to the shareholders' meeting:

- direct election of the chairperson or the board of directors;
- election and removal of the members of the compensation committee and of the independent proxy;
- delisting of the company's equity securities; and
- approval or rejection of the compensation of the board, the executive management and, if any, the advisory board.

The Board of Directors

The board of directors is responsible for the ultimate management and representation of the company. Its main duty is to determine the corporate strategy and allocate corporate resources (strategic governance). In general, the board is authorised to decide all matters that are not reserved to the shareholders' meeting or to the auditors by law or by the articles of association, or that are delegated to the executive management based on organisational regulations.

Statutory law lists certain fundamental matters specifically reserved to the board. The following board responsibilities are non-delegable and inalienable:

- the ultimate management of the company – in particular, the duty to determine the corporate strategy and allocate the corporate resources (strategic governance);
- defining the fundamental organisational structure;
- setting up an accounting and financial control system (including an internal control system for medium-sized and larger businesses) as well as financial planning as far as necessary to manage the company;
- appointing and removing the management as well as granting of signing authority to the

individuals authorised to act on behalf of the company;

- ultimately monitoring the individuals entrusted with management responsibilities, in view of compliance with the applicable law, the articles of association, regulations and directives;
- preparing annual business reports and shareholders' meetings as well as implementing their resolutions;
- issuing the annual compensation report on the board's and executive management's compensation (only for listed companies); and
- filing an application for a debt restructuring moratorium and notifying the bankruptcy court if the company's liabilities are no longer covered by its assets (over-indebtedness).

Notwithstanding the non-delegable and inalienable nature of these responsibilities, the board of directors may delegate the preparation and execution of its resolutions to committees, but not the decision-making itself (*"delegation of decision-shaping but not decision-making"*). Listed companies often establish an audit committee, a compensation committee and/or a nomination committee.

Statutory Auditors

The statutory auditors serve as a controlling body by (i) reviewing the annual accounts and the motions made by the board to the shareholders' meeting on the allocation of the balance sheet profit and by (ii) reporting to the shareholders' meeting whether the annual accounts comply with the statutory provisions, the articles of association and the applicable financial reporting standards.

3.3 Decision-Making Processes

The shareholders' meeting is convened by the board of directors. The notice must include the agenda items and the boards' motions (and

shareholders' motions, if any). The board of directors is required to briefly explain its proposals. In the case of shareholders' motions, there is an option, but not an obligation, to provide a brief explanatory statement. Resolutions can only be made on motions relating to agenda items that were duly notified (see **5.3 Shareholder Meetings**). In general, the absolute majority of the votes represented is necessary to pass a resolution and conduct elections.

Resolutions

For certain important resolutions (such as the amendment of the company's purpose, the introduction of conditional capital, of a capital band or of transfer restricted shares), the law requires a qualified majority – ie, two thirds of the voting rights represented and the absolute majority of the nominal value of shares represented. A requirement for a qualified majority may also be increased for other matters by a resolution of the shareholders' meeting which satisfies the proposed majority requirement.

With the entry into force of the company law revision, resolutions of the shareholders' meeting may now be passed in writing or by electronic means, unless a shareholder or its representative requests oral deliberation. In addition, the owners or representatives of all the company's shares may, if no objection is raised and provided that the owners or representatives of all the shares participate, hold a plenary meeting – ie, a shareholders' meeting without complying with the applicable regulations on convening meetings.

In most companies, the principle of *"one share, one vote"* applies. The articles of association may, however, also provide for voting shares. These can often be found in family-controlled companies, both private and listed.

Under Swiss company law, the board of directors' resolutions may be passed by a (relative) majority of the votes cast at the meeting. However, the articles of association and the organisational regulations may also introduce a quorum for the presence of a minimum number of board members or for a specific vote of the board. In the case of a tie, the chairperson holds the casting vote, unless the articles of association stipulate otherwise.

Resolutions of the board of directors may be passed in writing by way of circular resolution or electronically (without signatures), provided that no member of the board requests oral deliberation.

4. Directors and Officers

4.1 Board Structure

Swiss company law generally provides for a one-tier board model. In practice, however, day-to-day management (except for the non-delegable and inalienable competencies of the board, see **3.2 Decisions Made by Particular Bodies**) is common, and typically in listed companies, delegated from the board to an executive management, thereby leading to a two-tier board structure. Such rightful delegation excludes the directors' liability for damages relating to the delegated day-to-day management (but not the core duties) provided that the board applied the necessary care in selecting, instructing and supervising the management.

As a particularity and exception, banks and private insurance companies are required by law to establish a two-tier structure with a functional and personal separation of operative management and supervision.

4.2 Roles of Board Members

Swiss company law generally does not specify the roles of the members of the board of directors in much detail. These roles have to be specified in the organisation regulations.

Chairperson

The chairperson of the board should ensure the timely and appropriate information of the board members and the preparation of its meetings. The chairperson also:

- acts as a primary contact person to the executive management;
- chairs the shareholders' meeting;
- represents the company internally and externally; and
- generally ensures the proper functioning of the board.

As previously stated, the duties of the chairperson are usually further specified in the organisational regulations.

Even though the law does not explicitly mention the position of the vice-chairperson, it is advisable to appoint one in case the chairperson is unable to perform their duties. Again, the scope of the vice-chairperson's duties should be defined in the organisational regulations.

Other Appointments

In addition, the board of directors may appoint a secretary who does not have to be a board member. The secretary's duties are of a mere administrative nature relating to the board's tasks, such as taking minutes.

The SCBP also recommends the role of a lead independent director, particularly to prevent or address any potential conflict of interest situations. The lead independent director, an experi-

enced non-executive member of the board, may be appointed in the event that a single individual assumes the functions of chairperson and CEO. The appointment of lead directors is not uncommon for listed companies in Switzerland.

4.3 Board Composition Requirements/Recommendations

Regarding the composition of the board, current Swiss company law is flexible and the shareholders enjoy broad discretion. Swiss company law contains no rules on the maximum number of seats and no age restrictions on board members. However, listed Swiss companies must observe the newly implemented gender representation guidelines for the board of directors in listed companies (see 2.2 ESG Considerations).

Regulated Industries

In regulated industries – particularly in the financial sector – regulations require the members of the executive bodies of supervised institutions to grant assurance of proper business conduct and required knowledge and experience (*“fit and proper”*). According to FINMA, the main purpose of these requirements is to maintain public confidence in those institutions and to safeguard the reputation of the Swiss financial centre.

Assurance of proper business conduct covers matters of personal character (including criminal records) and professional qualifications required for the proper management of a supervised entity. The principal criterion used in assessing a person's suitability is their past and present business activity. As to the requirements regarding the composition of the board relating to independent directors, see 4.5 Rules/Requirements Concerning Independence of Directors.

4.4 Appointment and Removal of Directors/Officers

Only the shareholders may vote on the appointment or the removal of any of the directors. This is permissible whenever a shareholders' meeting is held and its agenda provides for the respective election or removal. Significant shareholders (see 5.3 Shareholder Meetings) are entitled to request the board to convene an extraordinary shareholders' meeting and put the requested items on the agenda.

For listed companies, the chairperson of the board of directors, each member of the board of directors and the members of the compensation committee must be appointed and (re-)elected individually and annually by the shareholders' meeting. In non-listed companies, the elected board members may resolve on the board's organisation, constitution and its members' functions, and notably may appoint the chairperson among its elected members without a shareholders' vote.

Unless otherwise provided by the articles of association, the shareholders' meeting passes resolutions on the election and removal of any director by an absolute majority of the votes represented at the respective meeting.

4.5 Rules/Requirements Concerning Independence of Directors

Swiss company law does not require business corporations to have independent directors.

The SCBP, however, emphasises that well-founded decisions can emerge only by exchanging ideas and critical views among the members of the board of directors and the executive management. Therefore, it recommends that the majority of the board should consist of independent members. Independent members are

deemed to be non-executive members of the board who:

- have never been a member of the executive management or, if they have, then more than three years ago;
- have never served as lead auditor or who served as lead auditor more than two years ago; and
- have no or only minor business relations with the company.

The board of directors may establish further criteria for independence. Importantly, in cases of cross-involvement with other boards, the independence of the member in question should be carefully examined on a case-by-case basis.

According to the SCBP, the nomination committee should be predominantly composed of independent directors. For the compensation committee, only independent members of the board of directors should be proposed for election by the shareholders. Members who have reciprocal board memberships – ie, a committee member responsible for co-determining the compensation of a member of the board of directors or the executive management under whose supervisory or directive authority the committee member serves in another company – should not be proposed.

Banking and Insurance

For banking and insurance entities, FINMA has issued rules in its circulars “*Corporate Governance – banks*” (2017/01) and “*Corporate Governance – insurers*” (2017/02). Pursuant to these rules, at least one third of the board of a banking entity must consist of non-executive and independent directors. Board members are generally considered to be independent if they are not (and have not been during the past two years)

engaged in any other function for the respective entity (including as auditor). Independent directors should not maintain significant business relations with the entity that could lead to conflicts of interest and/or should not act on behalf of significant shareholders.

Conflicts of Interest

The statutory duty of care and loyalty requires directors to perform their duties with due care and safeguard the company’s interest in good faith, including avoiding and properly addressing conflicts of interest. If a director fails to comply with its duty and favours personal interests over those of the company, any shareholder may hold such a director, and potentially the board, liable for any damage caused by such a breach of the duty of loyalty, and seek indemnification (for D&O liability claims, see 4.8 **Consequences and Enforcement of Breach of Directors’ Duties**).

Members of the board of directors and of the executive management should promptly inform the board of directors of any conflicts of interest affecting them. However, board members are not required to be completely “*disinterested*”; for the conflict to be considered relevant, it needs to be of a certain intensity. The board of directors must then decide on and take the appropriate measures required to safeguard the company’s interests. For an overview of such measures and further guidance, the SCBP can be consulted.

In practice, companies’ organisational regulations often provide for appropriate rules and measures in the case of a director’s conflict of interest (such as disclosure of conflict and possible abstention from voting and/or meetings).

4.6 Legal Duties of Directors/Officers

The board of directors is responsible for the ultimate management and representation of the

company. Its main duty is to determine the corporate strategy and allocate corporate resources (strategic governance). In general, the board is authorised to decide on all matters that are not reserved to the shareholders' meeting or the auditors (by law or by the articles of association), or that are delegated to the executive management based on organisational regulations.

Statutory law enumerates certain fundamental matters specifically reserved for the board for decision-making (see **3.2 Decisions Made by Particular Bodies** for more details).

4.7 Responsibility/Accountability of Directors

The board owes its fiduciary duties primarily to the company, and must represent it and act in its best interests. When determining the best interests of the company, the board, according to the prevailing legal opinion in Switzerland, should consider the long-term interests of the shareholders as well as those of other stakeholders, such as the company's employees or creditors.

4.8 Consequences and Enforcement of Breach of Directors' Duties

The board members and "*de facto directors*" (ie, persons not formally appointed as directors but who factually act as directors and significantly influence the company's decision-making process), as well as the members of the executive management, are liable for damages caused by intentional or negligent breach of their duties. As a rule, directors' and officers' (D&O) liability is joint and several, and each director may be held personally liable. Under the business judgement rule, as developed by Swiss case law, any business decision made without conflicts of interests in a proper and reasonably informed manner does not constitute a breach of obliga-

tions, even if it turns out to have been materially wrong in retrospect.

The expected level of care is generally assessed based on an objective standard. However, specialist knowledge may result in a higher standard when assessing the actions of an individual board member.

Liability Actions

D&O liability actions may be brought by the company, shareholders, and – in the event of bankruptcy, the company's creditors. Shareholders' actions can be direct, if they suffered direct damage, or indirect (as a derivative suit), if they seek to act on behalf of the company due to indirectly caused damages (ie, damage to the value of their shares resulting from damage suffered by the company). However, formal actions against board members are rather rare in practice. Many conflicts end with out-of-court settlements, frequently facilitated (and financed) by D&O insurers.

In addition, while Swiss company law contains some rules to address and ease the cost concerns that typically arise in the event of shareholder lawsuits, these rules do not effectively foster shareholders' actions, mainly because they are inapplicable to payments of advances to the courts. Finally, plaintiffs may also prefer actions against auditors, where deemed possible, in search of "*deep pockets*".

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In addition to the potential claims mentioned under **4.8 Consequences and Enforcement of Breach of Directors' Duties**, the board of directors or the executive management of listed companies may be subject to criminal sanctions pursuant to the Swiss Criminal Code, if

they pay or accept prohibited remuneration (see **4.10 Approvals and Restrictions Concerning Payments to Directors/Officers**). It follows that decisions on remuneration for the board and executive management and their subsequent payment or receipt, respectively, have to be carefully prepared in compliance with Swiss company law and related criminal law.

As a general principle, companies cannot validly preclude the liability of directors and executive management in advance. The annual shareholders' meeting may, however, grant discharge to the directors and the executive management for the preceding business year. As a result, the company and any shareholders who voted in favour of the resolution are precluded from bringing an action against the directors and executive management for any facts that were known to the shareholders' meeting at that time.

Often, companies seek D&O insurance coverage for their members of the board of directors and executive management.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

For private companies, it is generally the exclusive competence of the board to determine the remuneration of its members and of the executive management.

The Swiss Federal Supreme Court has consistently stated that remuneration must be justifiable in relation to both the company's overall financial situation and the relative contributions of the individual board members. This principle also derives from the duty of care and loyalty of board members, which only vaguely limits the board's discretion in determining the remuneration. The Swiss Federal Supreme Court exercises restraint

in reviewing remuneration decisions as it considers the companies' governing bodies to be best suited to address such issues.

Say-on-Pay

Swiss companies with shares listed on a Swiss or foreign stock exchange have to annually submit the board's proposal on executive compensation to the shareholders for a binding vote (binding say-on-pay). The shareholders' meeting has to vote separately on the proposed aggregate amount of compensation for each member of the board of directors, the executive management and, if any, the advisory board. However, in contrast to certain foreign legislations on executive pay, Swiss law does not impose a limit or maximum amount (cap) on remuneration.

Companies are required to specify the details of the vote on compensation in their articles of association. Various models are possible. For example, shareholders may vote on fixed compensation for the term until the next ordinary shareholders' meeting (prospective vote) or on performance-based compensation for the previous financial year (retrospective vote). Many major Swiss-listed companies include in their articles of association a provision for a vote on a compensation cap, whereby the shareholders vote in advance on the maximum amounts of compensation for the respective governing bodies for the upcoming business year (prospective vote). If variable remuneration is subject to a prospective vote, the remuneration report must be submitted to the shareholders' meeting for a consultative vote.

According to the revised SCBP, the board of directors may link variable remuneration to specific compliance and other sustainability objectives. Furthermore, the remuneration system should be designed in such a way that total

compensation is reduced if certain objectives are not achieved (“*malus*”). The remuneration system may also include a provision in the contracts with top executives that, beyond the legal requirements, reserves the right to claw back compensation that has already been paid under certain conditions (“*claw-back*”).

Specific types of executive benefits and compensations – such as loans, credits and pension benefits outside the occupational pension – require an explicit basis in the company’s articles of association. This also applies to the maximum terms and the maximum notice periods for service or employment agreements with members of the board of directors and of the executive management. In any event, notice periods or fixed contract terms exceeding one year are not permitted.

Certain types of compensation to members of the board and executive management – eg, sign-on bonuses that do not compensate for an actual financial disadvantage, non-statutory severance payments (“*golden parachutes*”), undue advanced compensation (“*golden hello*”) or certain types of transaction bonuses – are not allowed. The payment or receipt of such impermissible compensation by members of the board of directors, executive management, or advisory board (if any) is punishable by imprisonment and fines.

Special Requirements During Public Bids

Following the launch of a public takeover offer, any amendments to executive agreements with executive management members may qualify as defensive measures and as such may not be altered subject to the approval by the shareholders’ meeting and a review and approval by the TOB. Even in a pre-bid phase, the TOB may, as case law demonstrates, declare changes to

agreements of executive management null and void if fundamental principles of company law – in particular, the duty to act in the company’s best interests – are disregarded.

4.11 Disclosure of Payments to Directors/Officers

Privately held companies are not required by law to specifically disclose the remuneration, fees or benefits payable to their directors and executive management. For publicly held companies, however, Swiss company law requires the disclosure of the respective aggregate remuneration amounts for both the board and the executive management, the total compensation of each of the board members as well as the highest total compensation among the members of executive management (but not the specific compensation of the other members of executive management). All this information is to be disclosed in a separate audited compensation report to the shareholders.

The SIX Directive Corporate Governance extends the above-mentioned requirement to all issuers with a primary listing at the SIX Swiss Exchange (ie, with no other main listing) whether incorporated in Switzerland or not. In addition, it requires disclosure of information on the basic principles and elements of compensation and share-ownership programmes as well as of the method of its determination.

For banking entities, insurances, funds and branches thereof, FINMA has issued rules in its circular “*Remuneration Schedules*”. These rules contain the basic principles and general elements of compensation with regard to all employees, directors and officers of the company. However, implementation of these rules is only compulsory for larger banks and insurance companies.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

The shareholders' meeting is the paramount body of a company. The shareholders are entitled to elect and remove the board of directors and the statutory auditors.

Swiss company law grants shareholders a variety of rights, which can be categorised in (i) participation and (ii) property rights. These include the right to information and inspection as well as the right to determine dividends. The SCBP emphasises the importance of providing comprehensive information to shareholders to enable them to exercise their rights on a fully informed basis.

5.2 Role of Shareholders in Company Management

By statutory law, the management of a company is entrusted to its governing bodies (board of directors and executive management). Consequently, shareholders are not supposed to be involved in the management of the company (for their competences, see **3.2 Decisions Made by Particular Bodies**). Shareholders may, however, try to exert pressure and thus indirectly influence the decision-making process and actions of the board – for example:

- by formally requesting additional information or a non-binding vote in a shareholders' meeting on a specific issue that falls within the competence of the board; or
- by threatening or bringing removal motions relating to certain board members, or through shareholders' claims against the company to protect their rights, or against liable directors or officers to penalise non-compliance with statutory duties and to recover damages.

Some shareholder activists also use the media to make the relevant position of the (dissident) shareholder known to the public.

5.3 Shareholder Meetings

Ordinary and extraordinary shareholders' meetings are a core element of corporate governance in Switzerland. The ordinary shareholders' meeting takes place either physically, virtually, or in a hybrid form once a year within six months of the end of the financial year. The in-person meeting may also be held abroad if explicitly provided for in the articles of association and if the chosen venue does not make it unreasonably difficult for shareholders to exercise their rights. Provided that the interventions of the participants are broadcasted to all venues, it is also possible to hold a shareholders' meeting simultaneously at several venues in Switzerland and/or abroad.

At a hybrid shareholders' meeting, shareholders who are unable to attend the meeting in person may exercise their rights electronically. It is further possible to hold shareholders' meetings entirely virtually without an in-person meeting, provided that the articles of association contemplate this format.

Further, extraordinary shareholders' meetings may be convened as and when required.

Convening a Meeting

In general, the board of directors convenes the shareholders' meeting. In order to validly hold a shareholders' meeting, the notice convening the meeting must be given at least 20 days before such meeting date. Further, shareholder(s) of a listed company may request the convening of a shareholders' meeting, provided they hold at least 5% of the share capital or the voting power in the company. If the board of directors receives a request to convene a shareholders'

meeting, the board must act within an appropriate timeframe. In privately held companies, the convocation of a shareholders' meeting may be requested by shareholder(s) holding at least 10% of the share capital or the voting power in the company.

The notice must include the agenda items and the motions of the board of directors, and, if any, of the shareholders who have requested an extraordinary meeting to take place or solely requested an item to be placed on the agenda. These formal invitation rules may be disregarded in the case of a universal meeting, where all shareholders or representatives of all company shares are present.

Shareholder Participation

When holding the meeting, shareholders are entitled to participate and exercise their rights personally (see 5.3 Shareholder Meetings) or by a proxy. Shareholders of listed companies may also authorise an institutional proxy, the so-called independent proxy. Such an independent proxy needs to be elected by the shareholders' meeting and has to exercise the voting rights granted by the shareholders in accordance with their respective instructions. The independent proxy must keep the voting instructions of shareholders confidential. Where the shareholders' meeting has not appointed an independent proxy and there are no specific rules in the articles of association, the board should appoint one ahead of a next shareholders' meeting.

5.4 Shareholder Claims

Under Swiss company law, D&O liability actions may be brought against the members of the board and executive management by:

- the company;

- the shareholders (see 4.8 Consequences and Enforcement of Breach of Directors' Duties); and
- in the event of the company's bankruptcy, the company's creditors (see 4.8 Consequences and Enforcement of Breach of Directors' Duties).

5.5 Disclosure by Shareholders in Publicly Traded Companies

FinMIA requires that significant shareholders who acquire or sell equity securities (shares, any kind of rights to buy or sell including options or other financial instruments) of a Swiss-listed company (or foreign company primarily listed on a Swiss stock exchange) must notify the company and the stock exchange within four trading days if their holdings reach or cross any of the following voting rights thresholds: 3%, 5%, 10%, 15%, 20%, 25%, 33.33%, 50% or 66.66%. Within two additional trading days, the company must publicly disclose to the market any reports it has received concerning such changes in the ownership of its shares.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

All Swiss companies are obliged to prepare an annual report with the annual accounts, composed of the balance sheet, the profit and loss statement, and the notes to the accounts. Larger companies must additionally draw up a cash flow statement and a management report. In general, the annual report must be made available to the company's shareholders. In private companies, however, it does not have to be disclosed to the public.

SIX-listed companies must publish (by ad hoc announcement) audited annual reports and unaudited half-yearly interim financial reports in accordance with International Financial Reporting Standards or, where permitted within the respective trading segment, with alternative recognised accounting standards (such as US GAAP or Swiss GAAP-FER).

6.2 Disclosure of Corporate Governance Arrangements

In contrast to privately held companies, listed companies and their shareholders have to fulfil certain reporting and disclosure requirements provided for by the SIX Listing Rules, starting with a duty to disclose significant shareholdings (see 5.5 Disclosure by Shareholders in Publicly Traded Companies). Further requirements include the following.

Ad Hoc Publicity

As a rule, a listed company must immediately disclose to the market any non-publicly-known, price-sensitive facts that arise in connection with its business. A fact is considered price-sensitive if its disclosure is likely to cause a significant change in market prices and influence a reasonable market participant's investment decision (ex ante determination). A price change is deemed significant if it substantially exceeds the usual price fluctuations.

The SIX Listing Rules and the SIX Directive on Ad Hoc Publicity were partially revised in 2021, with the following main changes:

- the new regulations repeal the practice of per se price-sensitive information and leave the determination of whether information is price sensitive to the issuer (other than for the annual and interim reports);

- ad hoc announcements containing price-sensitive information must now be flagged as such (*"Ad hoc announcement pursuant to Article 53 SIX Listing Rules"*) and be made separately available and easily identifiable on the issuer's website; and
- additionally, issuers are required to implement adequate and transparent internal rules or processes to ensure the confidentiality of price-sensitive facts whose disclosure has been postponed.

Information on Management and Control Mechanisms

The SIX Directive Corporate Governance requires SIX-listed issuers to include in their annual report a separate corporate governance section concerning important information on the management and control mechanisms at the highest corporate level. Although information on remuneration is compulsory (see 4.10 Approvals and Restrictions Concerning Payments to Directors/Officers), other broad categories of information – such as group and capital structure, board of directors, auditors, shareholder participation rights, change of control or defence measures, and information policy – may be dealt with in accordance with the principle of *"comply or explain"*.

Management Transactions

The SIX Directive on the Disclosure of Management Transactions imposes obligations on listed issuers to disclose any buy-or-sell transactions concluded by their directors and members of the executive management (including related parties) in the respective issuer's equity securities or financial instruments. Each issuer has to ensure that its board members and executive management report each management transaction to the issuer within two trading days. The issuer has to publish the notified transaction

via the SIX electronic reporting platform for the disclosure of management transactions within three trading days following such notification; the report will be shown without mentioning the individual's name.

6.3 Companies Registry Filings

Swiss companies must file relevant corporate information and any changes thereto with the competent cantonal commercial registry. This includes amendments to the articles of association, such as a change to the corporate purpose, the capital structure, share transfer restrictions, and appointments to the board, as well as changes to other authorised signatories. This information is publicly available from the competent commercial registry. Filings must be made upon occurrence and are also published electronically in the Swiss Official Gazette of Commerce.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

Depending on the size of the entity, a company has to submit its accounts and financial statements to an ordinary (ie, full) audit or a limited audit. No audit requirement exists for smaller companies with less than ten full-time employees, if their shareholders unanimously resolve to opt out of the audit requirement. If there is an audit requirement, the company has to elect an appropriate qualified independent auditor. An ordinary audit of the annual accounts, and, if applicable, the consolidated accounts, is required for the following companies:

- public companies that trade their shares at a stock exchange, have bonds outstanding, or contribute at least 20% of the assets or of the

turnover to the consolidated accounts of a listed company;

- companies that exceed two of the following thresholds in two consecutive financial years – a balance sheet total of CHF20 million, sales revenue of CHF40 million, and/or 250 full-time positions on annual average;
- companies that are required to prepare consolidated accounts;
- where the company's shareholders who represent at least 10% of the share capital so request; or
- where the articles of association provide for it or the shareholders' meeting decides that the annual accounts are subject to an ordinary audit, even if the law does not require so.

An ordinary audit must be carried out by the elected external auditor. If the company is not subject to an ordinary audit, it has to submit its annual accounts for a limited audit. With consent of all shareholders, a limited audit may be waived if the company does not have more than ten full-time employees.

Auditors are accountable and may be liable to the company and to the shareholders and creditors for losses arising from any intentional or negligent breach of their duties.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Swiss financial reporting rules require that companies or groups of companies subject to an ordinary (full) audit (see 7.1 Appointment of External Auditors) undergo a review (to be confirmed by the auditors) regarding the existence of an appropriate internal control system. There are, however, no statutory requirements for the specific establishment and effective organisation of the internal control system. This responsibil-

ity lies with the board of directors. An exception applies to banks and private insurance companies, for which FINMA has set forth specific requirements regarding risk management and internal controls in the relevant circulars (*“Corporate Governance – banks”* and *“Corporate Governance – insurers”*, respectively).

Such companies additionally have to report on the company’s risk assessment process and the identified material risks in the management report accompanying the annual financial statements. These provisions should ensure that the corporate risk of medium-sized and large enterprises is regularly monitored and analysed. The ultimate responsibility lies with the board of directors, which has to evaluate material business-related risks in a forward-looking and systematic manner.

In addition, the SCBP also recommends that the board of directors should provide internal control and risk management systems that are suitable for the company; it should encompass risk management, compliance and financial monitoring. In addition, the effectiveness of the internal control system should be assessed by an internal audit.



Law and Practice

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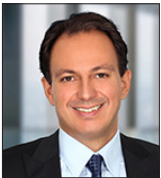
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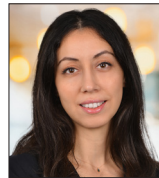
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**Balçioğlu Selçuk
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1. Introductory

1.1 Forms of Corporate/Business Organisations

Joint stock companies (JSC) and limited liability companies (LLC) are the preferred entity types for conducting commercial activities in Türkiye. They are both so-called capital companies, in which the shareholders are (save for specified exceptions) not liable for the company's debts and are hence limited to their capital commitments.

There most notable exceptions to this rule are: (i) some provisions allowing the lifting of the corporate veil, most prominently in the section of the Turkish Commercial Code (Law No 6102 or TCC) regulating company groups and affiliation, under Articles 202, 206 and 209; and (ii) solely in the case of LLCs, the shareholders' liability for unpaid public debts of the company.

An LLC is easier to maintain than a JSC and is set to be the more common legal form, whereas a JSC is intended for companies that aim to be or already are listed on a stock exchange. However, due to historic reasons (namely the impracticability and inflexibility of the rules applying to LLCs before 2012), JSCs are disproportionately popular in Türkiye.

Even today, a JSC is still preferred in cases where shareholders with potentially conflicting interests come together, such as in a joint venture. Also, in a number of sectors (such as banking, insurance and financial leases) only JSCs can operate.

The LLC would be more suitable when a simple and fully owned structure is desired.

1.2 Sources of Corporate Governance Requirements

The TCC is the main source, setting out the general rules applying to companies at the highest level. It is accompanied by an extensive set of secondary legislation (regulations, directives, and communiqués issued by the Ministry of Trade) setting out further details mostly relating to the practical implementation of the principles under the TCC.

There is a second law that sets specific additional rules for so-called public companies: the Capital Markets Law (Law No 6362). Public companies are (i) companies publicly traded on the stock exchange (listed companies) and (ii) companies that have more than 500 shareholders. The most prominent piece of secondary legislation applying to public companies is the Corporate Governance Communiqué numbered II-17.1 issued by the Capital Market Board (the "Communiqué"). With that said, secondary legislations and announcements of both the Turkish Capital Markets Board (CMB) and the *Borsa İstanbul* (Istanbul Stock Exchange) also regulate corporate governance requirements.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Corporate governance principles applying to listed companies are mainly regulated under the Communiqué. The Communiqué includes both mandatory requirements and non-mandatory requirements. Mandatory requirements are only imposed on listed companies. The exact requirements that are mandatorily applied to a company depend on its so-called corporate governance group. This in turn is determined by the CMB by taking into account the company's market value and market value of free-floating shares.

Examples of some mandatory requirements are:

- establishing an investor relations department;
- appointing a certain number of independent board members;
- establishing certain committees such as the audit committee, the corporate governance committee, and the early detection of risks committee;
- disclosing certain policies such as the remuneration policy for board members and executives;
- adhering to limitations imposed on related-party transactions; and
- adhering to limitations imposed on the establishment of pledges, or the granting of guarantees, on assets owned by listed companies.

Examples of non-mandatory principles that can be followed are:

- adhering to sustainability principles;
- not appointing the same board member to more than one committee; and
- providing, in the articles of association of the company, for clear separation between the authorities of the chairman of the board of directors and those of the chief executive officer.

Following these principles is voluntary, but non-compliant companies must provide an explanation for not doing so, in their annual corporate governance compliance reports.

In addition to corporate governance requirements regulated under the Communiqué, both public and non-public companies that have issued capital markets instruments except shares to the Turkish market must make certain public disclosures. Public disclosure require-

ments are regulated under the Special Events Communiqué numbered II-15.1.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In Türkiye, regulatory updates and compliance measures are tailored to address the country's unique economic challenges and conditions, including managing economic volatility. Significant efforts have also been made to align the country with the EU Green Deal. Green/sustainability reporting standards were made mandatory for large companies. Strides have been taken on the digital transformation front, including the “*National Technology Move*”, which aims to boost technological innovation and self-sufficiency, and various e-government projects aimed at modernising public services and enhancing digital governance. Additionally, efforts to improve board diversity and inclusion, such as increasing the representation of women and minorities on corporate boards, are designed to reflect Türkiye's specific cultural and social norms. Moreover, impact investing is becoming a hot topic amongst Turkish venture capital and capital markets circles. Another remarkable update is that the CMB has introduced regulations for the crypto-assets sector, subjecting crypto-assets companies intending to operate in Türkiye to high corporate governance standards similar to those imposed on financial institutions.

2.2 ESG Considerations

While many companies voluntarily adopt international standards, such as those of the Global Reporting Initiative or Sustainability Accounting Standards Board, to enhance their credibility and transparency, Türkiye introduced its own green/sustainability reporting standards in 2023. Companies listed in the applicable scope must

prepare and submit sustainability reports if they meet at least two of the following three thresholds in two consecutive reporting periods:

- total assets equal to or higher than TRY500 million;
- annual net sales revenue equal to or higher than TRY1 billion; and
- total number of employees equal to or higher than 250.

Banks must submit sustainability reports regardless of whether they meet any of these thresholds. One exemption is that banks owned by the Savings Deposit Insurance Fund are exempt from this requirement. Companies that do not fall within the scope of the regulation are not obligated to report but may do so voluntarily. Companies subject to mandatory reporting will be required to disclose all sustainability-related activities carried out in 2024, with reports to be submitted by 2025.

For listed companies, corporate governance sustainability principles (which are separate from the mandatory sustainability reporting standards) were published by the CMB, although compliance with the same is not mandatory. Listed companies must, however, disclose in their periodic corporate governance reports whether they adhere to the sustainability principles and explain the reasons if they do not. In addition, Türkiye has seen a growing trend towards increased awareness and voluntary adoption of international ESG standards among companies, driven by investor pressure and evolving global sustainability initiatives.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

A JSC is managed by its board (consisting of one or more directors) whereas an LLC is managed by one or more managers (ie, a board of managers). In each case these individuals/bodies are appointed by the shareholders.

Turkish company law follows a two-tier system. Accordingly, the management is placed in the hands of the board or the managers (depending on the company type), whereas shareholder matters are decided by the other mandatory body – ie, the “*general assembly*”. Each one of these bodies (management and shareholders) is endowed with a certain set of non-delegable powers and duties, constituting of a core set of powers and duties that can neither be moved from one to the other, nor transferred to another (voluntarily established) subcommittee, body or third (external) person.

Depending on whether companies meet the criteria determined under Decree 6434 on Determination of Companies Subject to Independent Audit, an independent auditor may also have to be appointed to the company.

3.2 Decisions Made by Particular Bodies

The board carries out all duties and actions whose competence is not explicitly granted to the general assembly by law or by the articles of association of the company. Meanwhile, the general assembly only acts on matters determined in the legislation and the articles of association of the company.

The management power belongs to all board members unless delegated.

Reserved Matters

According to the TCC, there are non-delegable powers vested in the board and general assembly of a JSC and LLC.

Board

Directors and managers of JSCs and LLCs cannot assign or waive some duties and authorities, including those that relate to the following:

- high-level management of the company;
- oversight of accounting and financial auditing;
- supervision of those who are authorised to manage the company;
- formation of risk detection committees; and
- appointment and dismissal of managers and persons performing duties similar to those of managers.

General assembly

The general assembly of a JSC and LLC cannot delegate certain duties, including the following:

- amendment of the articles of association of the company;
- appointment and dismissal of directors and managers, and determining their terms, remuneration and release;
- approving significant transactions (such as mergers, demergers or company-type transformations); and
- introducing or amending privileges granted to shares.

For public JSCs, there are additional matters reserved for the general assembly such as approving related-party transactions not approved by the majority of the independent board of directors and determining the upper limit of donations that can be made by the company.

3.3 Decision-Making Processes

General assembly meetings are called by the board, which determines also the agenda items to be discussed by the general assembly. But, with the approval of the shareholders present at the meeting, other items may be added to the agenda.

Please also refer to **5.3 Shareholder Meetings** regarding the conduct of general assembly meetings.

General Assembly of a JSC

Unless a higher quorum is stipulated under the articles of association, a simple majority of the votes will be sufficient to control the decision-making process of the general assembly of a JSC for most purposes. The TCC contains a limited number of super majority requirements for general assemblies. It is of course possible to tailor the articles of association to expand the list of super majority decisions or provide for higher quorum and voting requirements than those set forth in the TCC. The requirements set forth in the TCC can be made more stringent, but they cannot be made more lenient.

Under the TCC, quorum and voting requirements regarding the amendments to the articles of association are divided into four categories.

- Amendments to the articles of association aimed at:
 - (a) an increase of capital and increase of value of the upper limit of the registered capital, or
 - (b) a merger, demerger or change of legal form

require the presence of shareholders holding at least 25% of the share capital and can be adopt-

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ed with the simple majority of the shareholders present in the general assembly.

- Ordinary amendments of the articles of association require the presence of shareholders holding 50% of the share capital and must be adopted with a simple majority of votes represented in the general assembly meeting.
- Amendments to the articles of association concerning:
 - (a) a complete change of the field of activity of the JSC,
 - (b) issuance of privileged share,
 - (c) introducing restrictions to the transfer of registered shares, or
 - (d) a capital decrease or resolutions regarding the dissolution and liquidation of the company

must be adopted with affirmative votes of the shareholders representing at least 75% of the share capital (present or not).

- Amendments to the articles of association concerning:
 - (a) a change in the nationality of the JSC (ie, moving it outside of Türkiye), or
 - (b) imposing obligations on the shareholders other than capital contributions (ie, for the recovery of balance sheet losses or otherwise)

must be adopted with the unanimous vote of all shareholders (present or not).

Notwithstanding the foregoing, where there are different classes of shares in a JSC, any decision which adversely affects the rights of shareholders holding a specific class of shares will also need to be approved by a special assembly of such shareholders. At least 60% of the share

capital representing the privileged shares must be present at such a special assembly meeting.

General Assembly of an LLC

Unless provided otherwise in the articles of association, all general assembly resolutions must be adopted with a majority of the votes represented in the general assembly meeting. Therefore, the general rule in general assembly meetings of LLCs is that there is no quorum to convene the general assembly.

The following important decisions must be taken with (i) at least a two-thirds majority of the votes represented in the general assembly meeting and (ii) the majority of the votes representing the share capital:

- change of the field of activity;
- issuance of shares with privileged voting rights;
- restriction, prohibition or facilitation of share transfers;
- increase of capital;
- limitation of pre-emption rights;
- change of the registered address;
- approval by the general assembly to the activities of the shareholders or managers violating non-compete or loyalty obligations;
- bringing a lawsuit for dismissal of a shareholder on valid grounds and dismissal of a shareholder due to a reason stipulated in the articles of association; and
- dissolution of the company.

Unless more stringent requirements are stipulated in the articles of association, ordinary amendments to the articles may be adopted by a resolution of shareholders representing two thirds of the share capital. However, amendments to the articles of association concerning capital decrease must be adopted by the affirmative

votes of shareholders representing at least 75% of the share capital.

General assembly decisions regarding the following items must be taken with the unanimous votes of the shareholders:

- introduction or increase of additional payment obligations or secondary performance obligations; and
- amendments which introduce to the articles of association a reason for the dismissal of shareholders.

A lesser quorum cannot be set forth in the articles with respect to the foregoing decisions. However, a higher quorum requirement than stipulated by the TCC may be set forth in the articles of association.

Board of a JSC

Unless stated otherwise in the articles of association, the board shall convene with the majority of the number of directors and adopt resolutions with the majority of the directors present at the meeting. The articles of association cannot provide a quorum lower than stipulated in the TCC. Specific quorum and majority requirements for the board may be provided for in the articles of association.

Proxies are not allowed, but it is possible to pass a resolution without convening a meeting unless any of the directors requests a formal meeting. The board may approve the resolution separately, and signatures of the directors do not have to be on the same sheet.

Board of an LLC

The board of managers shall adopt resolutions by a majority vote unless otherwise provided in the articles of association. The chairman has the

tie-breaking vote. A different voting system for the board of managers can be set forth by the articles of association. Please refer to **4.2 Roles of Board Members** regarding the details of convening a board meeting.

4. Directors and Officers

4.1 Board Structure

The board (of directors in a JSC and of managers in an LLC if any) consists of a chairperson, a deputy chairperson, and the remaining members. Listed companies must have a certain number of independent board members.

The chairperson does not have a superseding power in a JSC, whereas if an LLC has more than one manager, the chairperson has the tie-breaking vote (if not determined otherwise in the articles of association of the LLC).

4.2 Roles of Board Members

Board members carry out the management function of the company as a whole. The main distinction between the members is the authority of the chairperson (and deputy chairperson) to call the board to a meeting.

Board meetings are in principle called by the chairperson (or in their absence the deputy chairperson). However, each board member can request a meeting in writing from the chairperson. The chairman must convene the meeting if the request is deemed appropriate. If the request is made by the majority of the board members, the chairperson has no such discretion and must convene the meeting within 30 days. If the chairperson or vice chairperson fails to convene a rightfully requested meeting, the requesting members can directly convene the meeting.

The board may delegate all of its delegable authority or a part of it to one or more directors or a third person with an internal directive if the articles of association of the company contain a provision allowing this. Management authority belongs to all the members of the board, taken in their entirety, unless specific arrangements and delegations are made.

4.3 Board Composition Requirements/Recommendations

The boards of JSCs and LLCs can have one or more members. For an LLC, at least one shareholder must be a manager (and thereby a member of the board). There is no such requirement for the board of a JSC.

Listed companies must have at least five board members. At least half of the board must consist of non-executive board members. One third of the board of directors of a listed company must consist of independent board members. Independent board members are also deemed non-executive board members. However, depending on the corporate governance group of the company or whether an exemption is granted by the CMB for the specific company, having only two independent board members regardless of the head count of the board of directors may suffice.

The board members may be foreign or Turkish nationals, and legal entities or real persons. The number of members on a board may be even or odd. Board members do not need to be employees of the company, but they can be.

For companies operating in specially regulated sectors, such as banking, the minimum number of, and other requirements for, board members can be specifically set out in the related legislation. Therefore, each company's board struc-

ture must be determined in compliance with the related applicable legislation.

4.4 Appointment and Removal of Directors/Officers

At incorporation, the initial board members must be appointed by being named in a temporary article of the articles of association.

Board members (and managers) are appointed and removed by the general assembly, at the latter's full discretion. However, if a board member of a JSC resigns, assuming that the remaining members still constitute a quorum for the board to take decisions, such remaining members can appoint an interim member, whose appointment would be approved and made permanent at the next general assembly meeting.

Appointment of independent board members in listed companies follows a different procedure. Independent board members must fulfil certain independence criteria. The nomination committee identifies candidates suitable for independent board members and submits them to the board of directors. If the board of directors approve the names, it then submits the proposed names to the CMB for comment. If the CMB does not disapprove of the names, the proposed independent board members may be appointed by the general assembly.

If a legal entity is appointed as a board member (or manager), it must designate one natural person representative to act on its behalf. The representative will be registered with the Trade Registry.

Generally, anyone may be appointed as board member. But some negative qualification criteria do exist (such as not being insolvent or incapacitated). Also, the board members of companies

acting in specific, regulated sectors, such as payment institutions and banks, must fulfil specific criteria set out under the related legislation (such as specific higher education achievement or not possessing a criminal record).

4.5 Rules/Requirements Concerning Independence of Directors

Standard Board Members

The board members of a JSC are prohibited from:

- participating in deliberations concerning matters in which a conflict of interest exists between themselves or their relatives and the company;
- entering into transactions with the company in their own name or on a third party's account without obtaining the permission of the general assembly;
- becoming indebted to the company in cash (unless they are shareholders); or
- competing with the company, unless the general assembly gives its consent otherwise.

Board members of an LLC are prohibited from engaging in activities which compete with the company, unless provided otherwise in the articles, or if all shareholders consent in writing.

For listed companies, in the event that controlling shareholders, board members, executives and their close relatives engage in a significant transaction that may cause a conflict of interest with the company, such transactions must be recorded in the general assembly minutes. The same requirement applies if the board members conclude business transactions or enter into partnerships falling into the company's field of activity.

Independent Board Members

Furthermore, an independent board member in a listed company must meet certain criteria to ensure impartiality and ability to act in the best interests of the company and its stakeholders. Most prominent amongst these independence criteria are:

- no employment or significant ownership ties to the company, its controlling shareholders or related entities within the past five years;
- no significant commercial relationships with the company or related entities within the past five years;
- possessing the necessary education, knowledge and experience to fulfil their duties effectively;
- not working full-time in public institutions, except for university faculty positions;
- being a resident of Türkiye;
- demonstrating strong ethics, possessing a professional reputation, and having the ability to maintain impartiality in conflicts of interest;
- having sufficient time to dedicate to the company's business and fulfil their responsibilities;
- serving on the company's board for no more than six years within the past decade;
- serving as an independent board member on no more than three companies controlled by the same shareholders and no more than five public companies in total; and
- not being registered as a board member representing a legal entity.

4.6 Legal Duties of Directors/Officers

A board member has the following obligations stipulated by law, for both JSCs and LLCs:

- the duty to act diligently;
- the duty of loyalty;

- the duty of equal treatment of shareholders under equal circumstances;
- convening a general assembly when a significant portion of the share capital is depleted; and
- establishing a committee for early determination and management of risks.

Additional obligations may be imposed on the members of the board by the articles of association.

Please also refer to **3.2 Decisions Made by Particular Bodies**.

4.7 Responsibility/Accountability of Directors

The directors in JSCs and managers in LLCs are primarily responsible towards the company. While there are ways for shareholders and creditors to enforce direct claims against them, this occurs as an extension of their duty of loyalty towards the company itself. In other words, the possibility of making such claims does not establish a direct duty of loyalty towards shareholders or creditors. In the context of group companies, claims can be made by additional parties (for example, the shareholders or creditors of the company's subsidiary), but these also do not construct a direct duty of loyalty.

In JSCs that have issued capital markets instruments (which includes any listed companies), the board of directors is responsible for preparing accurate financial tables and reports. Board members responsible for preparing financial tables and reports must provide an undertaking to guarantee the truth and accuracy of the financial tables and reporting.

Other officers are mere employees and are liable only to the company and under their employment agreements.

4.8 Consequences and Enforcement of Breach of Directors' Duties

If a director faultily breaches their obligations under the law or the articles of association and causes damage to the company, the company itself, its shareholders or creditors of the company may bring an indemnity claim against such director.

For companies that have issued capital markets instruments (other than shares), investors in such capital market instruments may bring claims against directors even though they are not shareholders.

If listed companies do not adhere to the corporate governance requirements, the CMB is authorised to adopt resolutions and take the necessary steps to enforce adherence to the corporate governance rules. If the board of directors or the general assembly of a company do not follow the CMB's instructions to achieve compliance with the corporate governance requirements, although the board of directors has sufficient members to resolve on such points within the 30-day grace period to be provided by the CMB, the CMB may appoint a sufficient number of independent board members to adopt necessary resolutions and take the steps necessary to achieve compliance with corporate governance rules.

In addition, if a public company incurs losses five years in a row, all privileges granted to shares in terms of voting rights and representation at the board of directors can be removed by the CMB.

For some breaches of law, the administrative fines can be enforced by the local authority and even imprisonment is threatened (although the latter is not generally enforced).

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

The legal representatives of a JSC (including the directors and other officers with the power to manage and represent the company) may be held personally liable if a JSC does not or cannot pay its tax debts.

In companies that have issued capital markets instruments, the board members may also be held liable for statements provided under the prospectus or issuance certificate and the true and accurate reporting of financial information.

Any liability by a director (or manager) requires a faulty action leading to damages. Therefore, if damages are not caused by the fault of the concerned director or manager, such person cannot be held liable.

If a management function is partially or completely delegated, the board will be released from liability to the extent of the delegated function. However, directors will be held liable if they have not selected or fail to monitor the relevant person with due care.

The liability of a present or former director or officer can be terminated either by an explicit release by shareholders' decision or through shareholder approval of the company's annual report and financial statements.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Directors and managers of a JSC and an LLC may be paid a special remuneration (called honorarium) if this is approved by a general assembly resolution. This is a non-delegable power of the general assembly. Other financial benefits (dividend shares) paid to directors will be subject to the same restriction, but if the relevant person is employed at the company, salaries so received will not have to be approved by the general assembly.

Without a valid general assembly resolution, the honorarium payments to the board members will not be lawful and could be reclaimed by the company. Also, the shareholders and creditors could file a damages claim. Finally, there is a risk of such payments being qualified as salaries by social security institutions, which could treat this as an evasion of social security payment obligations.

Listed companies have a remuneration policy, prepared by the remuneration committee and adopted by the board of directors of the public company. On the basis of this policy, the remuneration committee and the board of directors make suggestions for the remuneration of the board members to the general assembly. The general assembly ultimately resolves on the remuneration of the board members in line with the remuneration policy.

4.11 Disclosure of Payments to Directors/Officers

For non-public companies, remuneration policy does not need to be announced or disclosed, as the authorising general assembly resolution would not be subject to registration with the trade registry.

The remuneration policies of listed companies must be announced on both the company website and the public disclosure platform.

Note that companies that are not listed but are active in specifically regulated sectors have disclosure obligations towards their overseeing authorities/institutions. For example, payment institutions must share such information with the Turkish Central Bank at specific intervals.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

As per the so-called sole-obligation principle that applies to JSCs, save for very limited exceptions stipulated in law, no obligation can be imposed on the shareholders other than the obligation to pay the share subscription price and (if any) the premium. The primary obligation of a shareholder is to pay the outstanding portion of its capital subscription in due time.

JSC shareholders are not bound by a non-compete obligation towards the company. As for LLCs, shareholders have an obligation to refrain from actions that are to the detriment of the company, and specifically cannot carry out actions for their own benefit which do damage to the company. If foreseen under the articles of association of the LLC, shareholders may be prohibited from actions that compete with the company.

The TCC and the articles of association of the company govern the relationship between the shareholders and the company.

For JSCs, as a rule, share transfers are not subject to registration with the trade registry.

Therefore, for the purpose of identifying the shareholders of a JSC with certainty, it is necessary to examine the company's share ledger and the share certificates. However, if the JSC's shares are represented by bearer certificates, their transfer must be registered with the Central Securities Depository, whose records are not open to the public.

With that said, the names and share ownership of each shareholder is registered and published with the trade registry at the time of incorporation and after each capital increase or decrease, giving some level of publicity to the shareholding structure.

In addition, a notification to the trade registry is required when a shareholder's (direct or indirect) shareholding in a JSC exceeds the thresholds of (i) 5%, 10%, 20%, 25%, 33%, 50%, 67% or 100% or (ii) when a shareholder becomes the sole shareholder of a JSC. Public companies are subject to additional disclosure requirements where a group of shareholders' control over the company reaches or falls below certain thresholds (5%, 10%, 15%, 20%, 25%, 33%, 50%, 67%, or 95%). Please refer to **5.5 Disclosure by Shareholders in Publicly Traded Companies** for detailed information.

For LLCs, shareholding information and changes are registered in the trade registry and hence accessible to the public through the trade registry gazette. Shareholding records of publicly traded JSCs are kept by the Central Securities Depository. As said before, Central Securities Depository records are not public. With that said, listed companies must disclose their shareholding structure on the public disclosure platform every six months. The declared shareholding structure must be cleared of any indirect shareholdings and cross-shareholdings and must clearly indi-

cate the names of natural person shareholders owning more than 5% of shares. There are also disclosure requirements for major shareholding changes and control changes; please refer to **5.5 Disclosure by Shareholders in Publicly Traded Companies** for more information.

5.2 Role of Shareholders in Company Management

The non-delegable duties (reserved matters) of the general assembly, mentioned in **3.2 Decisions Made by Particular Bodies**, constitute the general assembly's main role in the company. In this light, the general assembly is obliged to take on the management of its reserved roles, while refraining from interfering in matters that fall under the board's non-delegable duties.

Unlike in a JSC, where representatives of the company are appointed by the board, in an LLC the general assembly may also appoint representatives of the company.

5.3 Shareholder Meetings

An ordinary general assembly must convene within three months as of the end of each financial year. General assembly meetings are called by the board.

Unless a higher quorum is stipulated under the articles of association of the company, pursuant to the default TCC provisions, simple majority shareholding will be sufficient to control a JSC for most purposes.

The TCC contains a very limited number of super majority requirements for general assemblies and decisions. It is possible for the shareholders to add to the list of super majority decisions or provide for higher (but not lower) quorum and voting requirements than those set forth in the TCC.

Please refer to **3.3 Decision-Making Processes** for further details on the invitation to these meetings, and the decision-taking quorum.

During the meeting, the meeting minutes are held and signed by the shareholders. A list of attendees is signed by those present at the meeting. For JSCs, this includes a board member. If the company has a single shareholder, the list of attendees does not have to be prepared.

5.4 Shareholder Claims

The shareholders may bring a claim against the directors if the directors breach their obligations under the law or the articles of association with fault, and if in doing so they cause damage to the shareholders.

Shareholders are entitled to bring a claim against the company for the cancellation of general assembly resolutions and board resolutions based on grounds specifically listed under the TCC.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Shareholders (including groups of shareholders acting in concert with each other) must disclose when they reach or fall below certain thresholds (5%, 10%, 15%, 20%, 25%, 33%, 50%, 67% or 95%) of the share capital or total voting rights, whether directly or indirectly. For direct shareholding changes, the Central Securities Depository (MKK) makes the relevant disclosure. For shareholding changes that are indirect or a result of acting in concert or changes in voting rights triggering the thresholds, the relevant investors must make the disclosures themselves.

Shareholders (including groups of shareholders acting in concert with each other) owning more than 20% of the company's shares or sharehold-

ers who are in possession of privileged shares to appoint or nominate at least one board member must submit a share sale information form to the CMB for approval before selling shares corresponding to more than 10% of the company's capital in a 12-month period. The same obligation applies to converting more than 10% of the company's non-tradeable shares into tradable shares.

Shareholders owning 10% or more of the shares in a company, directly or indirectly, or shareholders who are in possession of more than 10% of the privileged shares to appoint or nominate at least one board member also have the obligation to make a special events disclosure if they obtain any non-public insider information not known by the company.

While the capital markets legislation does not use the term “*ultimate beneficial owner*”, listed companies must disclose their shareholding structure every six months. The declared shareholding structure must be cleared of any indirect shareholdings and cross-shareholdings and must clearly indicate the names of natural person shareholders owning more than 5% of shares.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

An ordinary general assembly must convene within three months as of the end of each financial year. During this meeting, among other items, the approval of the annual report, financial statements and the dividend distribution are discussed. Ordinary general assembly meetings are not subject to registration, and such annual reports and financial statements are not

announced. However, the announcement and reporting requirements of listed companies and companies active in specifically governed sectors are highly regulated.

6.2 Disclosure of Corporate Governance Arrangements

For companies that are not listed, in principle, such disclosures are not required. As an exception, control agreements (establishing control by one company over another) must be registered with the trade registry and announced on the Trade Registry Gazette in order to be valid.

On the other hand, listed companies are subject to strict disclosure and transparency measures. Such disclosures are made on the company's website and the public disclosure platform.

6.3 Companies Registry Filings

Companies are registered with the trade registry, and the registration processes are carried out by the provincial or district trade registry directorate where the company's headquarters are located. Additionally, trade registry records are kept electronically under the Central Registry Record System (CRRS) and all trade registry procedures, applications and registrations are also completed online through CRRS.

Certain actions within a company require registration with the trade registry, before which the company is registered. These actions include, among others, amending the company's articles of association (including changing the share capital of the company), adopting an internal directive regarding the representation of the company, and changing the company's registered address. Such actions are effective upon registration with the trade registry, as stipulated under the TCC. Therefore, in order to effect the

actions that require such registration, filings must be made.

The registrations made with the trade registry are announced in the Trade Registry Gazette, which is publicly available. Such announcements only include the content that is subject to the registration, while additional documents are often submitted during the registration application. These additional documents, such as a power of attorney used during the transaction, remain in the company's registry files, and may be reviewed by those who request to review the relevant file at the trade registry.

Trade registry directorates are responsible for examining whether the conditions required for registration are met in each application. If any deficiencies are identified, the directorate may grant a specific period for the applicant to correct them. The trade registries also hold the authority to partially or fully reject registration requests in case of non-compliance. Additionally, if a trade registry directorate becomes aware that a registrable event has not been submitted by the responsible party, it may summon the relevant person to file the application within thirty days or to prove that there is no obligation to register.

A person who fails to submit a registration application within the period granted by the directorate and does not provide reasons for non-compliance shall be subject to an administrative fine. Failure to apply within the given period, or presenting insufficient justification for non-compliance, will result in the trade registry directorate referring the matter to the competent commercial court of first instance. Furthermore, third parties may report it to the directorate if they believe that a registration decision or action does not reflect the truth, is unlawful, contradicts public order, or may mislead others. In

such cases, the trade registry directorate may ask the third party to answer questions in writing or verbally, and failure to provide adequate responses may result in the complaint not being considered.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

As per Decree 6434 on Determination of Companies Subject to Independent Audit (the "Decree"), companies that – alone or together with their affiliated companies and subsidiaries – meet at least two of the following conditions in two consecutive fiscal periods are subject to independent auditing:

- total assets equal to or higher than TRY300 million;
- annual net sales revenue equal to or higher than TRY600 million; and
- total number of employees equal to or higher than 150.

Companies listed explicitly in Appendix I to the Decree (such as banks, financial leasing companies or investment companies) are subject to independent auditing regardless of the above-mentioned thresholds. Also, companies listed in Appendix II to the Decree (such as the companies operating in the energy sector with a licence or media service provider companies that own national, satellite and cable channels) are subject to independent auditing if such companies satisfy certain conditions specifically provided for them.

The independent auditor is tasked with auditing the financial statements and periodic auditing of the inventory and accounting, risk commission's report and annual reports of the board. The audi-

tors then provide a report, which could have one of the following conclusive opinions: affirmative, qualified affirmative, negative, or abstention.

In the case of a negative opinion or an abstention report, the board will be required to call a general assembly meeting within four business days as of the receipt of the opinion of the independent auditor and resign effectively as of the date of the general assembly meeting. The financial statements and the annual report have to be drafted again within six months by the new board to be appointed by the general assembly.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

One of the non-delegable duties of the board, and hence the directors, is setting up necessary arrangements for the accounting, financial auditing and financial planning (if required for the management of the company). This duty is an extension of the directors' duty to establish an internal control mechanism. Additionally, it is among the non-delegable duties of directors to establish an early detection and management of risks committee.

Listed companies are obliged to establish an expert committee, and operate and develop a system, in order to ensure early detection of threats to the existence, development and continuity of the company; to implement the necessary measures and remedies; and to manage the risk. In other companies, this committee is established immediately if the auditor deems it necessary and notifies the board in writing.

Trends and Developments

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Balcioğlu Selçuk Eymirlioğlu Ardiyok Keki Attorney Partnership is an Istanbul-based full-service law firm led by experienced professionals since 2007. Drawing on broad experience gained at Turkish and global law firms and international organisations, the firm has a strong team of almost 100 lawyers and economists, each well-equipped to provide creative and diligent transaction counselling and cutting-edge legal services. The firm's practice areas include corporate and M&A, competition and antitrust, banking and finance, energy, arbitration, competition, dispute resolution, intellectual property, joint ventures, regulatory and

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Digitisation of Corporate Books

2025 was marked by a digitisation trend in corporate maintenance.

Corporate resolution books and share ledgers were traditionally kept in paper form. As of 1 January 2026, all newly established companies will be required to maintain their non-accounting corporate books, including the share ledger, board of directors' resolution book, managers' resolution book, and general assembly meeting book, in electronic format.

Companies in regulated sectors such as banks, financial leasing and factoring companies must maintain their corporate books electronically as of 1 July 2025.

Existing companies that are not subject to the mandatory requirement may voluntarily adopt the electronic book-keeping system. However, once the transition is made, reverting to physical books will no longer be possible.

This development is a welcome addition and will increase speed and security in corporate maintenance tasks.

Accessing the Central Registry Record System (CRRS) Via E-Government Mandatory for Domestic Users

Trade registry applications are made online through a system called Central Registry Record System (CRRS). Login to this portal was possible for both domestic users (Turkish citizens or work-permit holders) and foreign users via username and password credentials until 14 April 2025. This allowed users to share account access simply by sharing login credentials. However, as of 14 April 2025, domestic users may only access their CRRS accounts via e-government portal or mobile signature.

Domestic users who are authorised representatives of companies and wish to authorise a third party to perform CRRS transactions on their behalf must grant authorisation to such third parties to initiate changes and/or submit them for approval in the CRRS system.

Green/Sustainability Reporting Standards

Türkiye introduced green and sustainability reporting standards, marking a key advancement in aligning corporate practices with environmental, social and governance (ESG) objectives. Under the new framework, companies that meet at least two out of three specific thresholds in two consecutive reporting periods are required to prepare and submit sustainability reports:

- total assets equal to or higher than TRY500 million;
- annual net sales revenue equal to or higher than TRY1 billion; and
- total number of employees equal to or higher than 250.

The regulation applies primarily to investment institutions supervised by the Capital Markets Board and joint stock companies who have issued capital markets instruments, and banks. Banks are obligated to comply with the reporting requirements regardless of whether they meet these thresholds. One exception is that banks owned by the Savings Deposit Insurance Fund are explicitly exempt from this obligation. While companies outside the mandatory scope are not required to report, they are permitted to do so voluntarily. Companies subject to mandatory disclosure must report on their sustainability-related activities undertaken during 2024, with submissions due in 2025.

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Challenges in E-Signature and Financial Seal Acquisition for Foreign Company Representatives

The transition to electronic statutory financial books requires companies to obtain a financial seal, which is executed using a secure electronic signature (e-signature) by the company representative. A secure e-signature is the only legally recognised form of electronic signature under Turkish law with the same effect as a wet-ink signature. These e-signatures can only be issued to natural persons through licensed service providers, following a KYC process. As the financial seal system is fairly new, further regulations are expected, and the details of how the implementation will progress remain unclear.

Term of Office of the Chairman and Vice Chairman of the Board of Directors Aligned With the Board's Term of Office

In 2024, an amendment to Article 366 (1) of the Turkish Commercial Code (TCC) introduced a significant change regarding the term of office for the chairman and vice chairman of the board of directors. Previously, companies were required to elect the chairman and vice chairman from among the board members on an annual basis, creating a recurring administrative obligation regardless of the board's overall term. With the new regulation, this annual re-election requirement has been abolished. Now, the chairman and vice chairman may be appointed for a term of up to three years, aligning their term of office with the maximum term permitted for members of the board of directors.

Change in Minimum Share Capital Requirements

The Presidential Decree on the Increase of the Required Minimum Capital Amount for Joint Stock and Limited Liability Companies was pub-

lished in the Official Gazette on 25 November 2023 and came into effect as of 2024.

With this Decree:

- the minimum share capital of limited liability companies was increased from TRY10,000 to TRY50,000;
- the minimum share capital of joint stock companies was increased from TRY50,000 to TRY250,000; and
- the minimum share capital of non-public joint stock companies that have adopted the registered capital system was increased from TRY100,000 to TRY500,000.

Whilst the increase rate looks drastic, the respective minimum amounts are still low when compared to the real needs of businesses. The earlier minimum share capital amounts had remained unchanged since back in 2012 and had been deteriorating in real value.

With the addition of a temporary article to the Turkish Commercial Code, which entered into force on 29 May 2024, the following apply.

- Joint stock companies and limited liability companies whose capital is below the minimum capital requirement must increase their capital to the amounts specified above by 31 December 2026, otherwise they will be deemed dissolved. The Ministry of Trade may extend this period by one year maximum, twice.
- Non-public joint stock companies that have adopted the registered capital system with a minimum issued capital of TRY250,000 shall be deemed to have withdrawn from this system if they fail to increase their initial capital and issued capital to TRY500,000 by 31 December 2026.

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- No quorum shall be required for general assembly meetings convened to increase the capital to the amounts specified above. Resolutions shall be taken by a majority of the votes present at the meeting, and no privileges may be exercised against such resolutions.

Amendments to the Rules on Technical Insolvency

The consequences of a deterioration of the financial status of joint stock companies and limited liability companies are regulated in the section titled “*Responsibilities and Authorities of Board of Directors*” of the TCC, and in a specific communiqué regulating the implementation of the corresponding provisions of the TCC (the “*Communiqué*”).

In this context, a company’s assets minus its liabilities on the one hand are measured against its share capital plus its legal reserves on the other. Any shortfall of the former position against the latter will be deemed a depletion (also called a loss) of the share capital.

The legal implications of such depletion and the relevant responsibilities of the board of directors (the “*board*”) vary depending on what percentage of the share capital was lost.

If half of the share capital is depleted, the board must immediately convene the general assembly. At such general assembly meeting, the board must provide a detailed explanation of the financial situation of the company, reasons for the loss and the measures which may be taken for the reduction of the loss and for the recovery. Thereby, a process is initiated which alerts the shareholders to the danger and enables them to take the actions necessary to improve the financial position of the company.

If two thirds of the share capital is lost, the company will be deemed in technical insolvency and the board must immediately convene the general assembly. In this case, the general assembly can decide on certain measures to fix the technical insolvency, by:

- decreasing the share capital, in order to bring it down so that the ratio of the lost share capital is improved to an acceptable level;
- increasing the share capital, so as to increase the assets position of the company, again with the same objective;
- making a capital replenishment, whereby the lost share capital is replenished without any new shares being issued (leading to the same outcome); or
- a combination of the above-mentioned measures.

If the general assembly does not resolve to enact any measure and omits to fix the technical insolvency, the company will enter into a dissolution procedure, which will most likely trigger an insolvency.

If there are strong indications that the company is heavily indebted, the board must prepare two sets of “*special purpose interim balance sheets*”: one set on a going-concern basis, and one set based on the predicted disposal values of the assets. If these interim balance sheets show that the assets of the company do not adequately cover its debts to its creditors, the board must immediately notify the competent court and file for bankruptcy of the company. This may be avoided, if creditors of the company representing a sufficient number of debts agree to subordinate their receivables to the receivables of the other creditors.

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The pandemic and the heavy devaluation of the Turkish lira over recent years have led to a situation in which a great number of companies have found themselves in distress. This in turn has prompted significant adjustments to the Communiqué regulating the details of the depletion of share capital. Specifically, two critical provisions were introduced by Temporary Article 1 of the Communiqué on the Procedures and Principles Regarding the Implementation of Article 376 of the TCC No 6102.

Exclusion of unrealised foreign exchange losses

Unrealised foreign exchange losses stemming from foreign currency liabilities were excluded from the calculation of the loss of share capital. This measure aimed to mitigate the adverse impact of the currency devaluation on companies' financial positions, allowing them to avoid being classified as technically insolvent solely due to exchange rate fluctuations.

Partial exclusion of certain expenses

Half of the sum of expenses incurred from leases, depreciations and personnel expenses accrued during the years 2020 and 2021 will not be considered in determining whether or not a company was in technical insolvency. This adjustment recognised the extraordinary economic challenges faced by businesses during this period, particularly exacerbated by the currency devaluation and its associated financial strains.

Effect of the temporary provisions

These provisions aimed to provide temporary relief to companies affected by the Turkish lira devaluation, enabling them to maintain their operations and financial viability despite facing significant economic headwinds. They proved somewhat successful in that a potential wave

of insolvencies was largely avoided. But, on the downside, this has likely resulted in many financially unhealthy companies still being in business. Pursuant to the legislative amendment enacted on 25 December 2024, it has been resolved that these two provisions shall remain in force until 1 January 2026.

Restrictions on the Use of Foreign Currency

The Presidential Decree numbered 32 on the Protection of the Value of Turkish Currency is a fairly old piece of legislation (dating back to 1989) aiming at stabilising the currency and managing the foreign currency environment in Türkiye. It, and its secondary legislation in the form of communiqués, had already undergone several changes over the years.

The Turkish lira came under devaluation pressure especially starting from 2018. As a response to that, changes were made to the secondary legislation implementing the aforementioned Decree as part of a broader strategy to protect and stabilise the Turkish lira by reducing reliance on foreign currencies in domestic transactions and encouraging the use of the national currency. A catalogue of transactions and contracts were identified which, starting from 2018, must be denominated in Turkish lira. These include service agreements, rental agreements, loan agreements, sales contracts for movable and immovable properties, and employment contracts. The list is fairly comprehensive and includes exceptions to this rule such as situations where products or services are sourced from suppliers abroad or where the debtor is foreign or foreign-owned. Also, some special consideration is applied to defence contracts or contracts made by the state.

On 6 March 2025, Communiqué (Communiqué No: 2025-32/72) amending the Communiqué on

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the Protection of the Value of Turkish Currency (Communiqué No: 2008-32/34) was published in the Official Gazette and became effective on the same day.

Under the old Communiqué No: 2008-32/34, the purchase price of movable property sale agreements (excluding vehicle sales) between Turkish residents could be determined in foreign currency, but payments were required to be made in Turkish lira. With this amendment, this requirement was eliminated, allowing payments to be made directly in foreign currency when the purchase price is determined accordingly. As a result, the sale of movable property agreements, particularly asset purchase agreements and share purchase agreements between Turkish residents, are allowed to be settled in foreign currency without restriction. However, the requirement to determine and settle the price in Turkish lira remains in effect for vehicle sales agreements between Turkish residents.

Risk Management and Internal Control Mechanisms

In recent practice, the leading points of discussion have revolved around how to best ensure and apply risk management and internal control mechanisms. Corporate governance-related discussions in Türkiye have increasingly focused on these critical areas, highlighting their importance in navigating a complex and dynamic business environment.

Role of the board and management

The board and senior management play pivotal roles in overseeing risk management. Under the TCC, it is among the non-delegable duties of the board of any listed company to establish an early detection and management of risks committee. For non-listed companies, such a committee can be set up if requested by the independent

auditor. Hence, the board sets the risk policies and ensures alignment of actions and measures with these policies, while continuous communication between the board, management and risk teams ensures effective risk-handling.

Another non-delegable duty of the board, for both joint stock companies and limited liability companies, is to make the necessary arrangements for accounting, financial auditing and financial planning of the company, if required for its management. To fulfil this duty, the board may need to establish internal control mechanisms within the company. Effective internal control systems are essential for safeguarding assets, ensuring financial reporting accuracy, and promoting operational efficiency. These systems help in detecting errors and fraud, ensuring compliance with laws and regulations, and achieving the organisation's goals.

Regular assessments and updates of internal control systems are necessary to respond to emerging risks. The board must lead this effort by acting through its directors or managers, or forming committees and delegating these duties with care. The actions to be carried out involve periodically reviewing and adjusting control activities to ensure they remain effective in addressing current and potential risks. The dynamic nature of business environments and evolving regulatory landscapes require continuous monitoring and improvement of these controls. By maintaining robust internal control mechanisms and fostering a culture of risk awareness, companies can enhance their resilience and operational stability.

Bolstering Anti-Money Laundering Measures

In recent years, Türkiye has significantly sharpened its anti-money laundering (AML) legislation and practices with the aim of combating finan-

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cial crimes and aligning with international standards. This shift reflects the nation's commitment to enhancing financial integrity and addressing the recommendations of global organisations such as the Financial Action Task Force (FATF).

Legislative enhancements

Amendments to existing laws

Law No 5549 on Prevention of Laundering Proceeds of Crime was amended to close gaps and address new challenges in relation to money laundering activities. These amendments have expanded the scope of predicate offences and increased penalties for non-compliance. They address not just traditional financial crimes but also offences such as tax evasion, corruption and environmental crimes. By expanding the scope of predicate offences, a wider array of illicit activities that could generate laundered funds should be covered.

Adoption of new regulations

New regulations have been introduced to enhance the legal framework for AML. These include detailed guidelines on customer due diligence, reporting suspicious transactions, and record-keeping requirements. The new regulations also mandate stricter verification processes for politically exposed persons and beneficial ownership disclosures.

Institutional strengthening

Financial Crimes Investigation Board (MASAK)

MASAK, Türkiye's financial intelligence unit (FIU), has been given more authority and resources to investigate money laundering activities. MASAK has enhanced its analytical capabilities and increased its collaboration with domestic and international agencies. MASAK collaborates with banks during their account opening process for new and/or foreign customers. The account opening process is now subject to the procure-

ment of more information and documents, with higher scrutiny when reviewing the same.

Enhanced supervision and enforcement

Regulatory bodies such as the Banking Regulation and Supervision Agency and the Capital Markets Board have intensified their supervision and enforcement activities. These agencies conduct more frequent inspections and impose heavier fines and sanctions on institutions that fail to comply with AML regulations.

Increased reporting and transparency

Mandatory reporting requirements

Financial institutions and other obligated entities are now required to report suspicious transactions more rigorously. A notable increase has been observed in the volume of suspicious transaction reports submitted to MASAK.

Beneficial ownership disclosure

New regulations require companies to disclose their ultimate beneficial owners, enhancing transparency and making it more difficult for individuals to hide illicit funds behind complex corporate structures. As mentioned above, this comes into play in practice in dealings with banks and opening new bank accounts, where detailed ownership structure charts and supporting documentation are requested.

International co-operation

Türkiye has worked to align its AML regulations with the FATF's recommendations. This includes implementing measures to prevent the financing of terrorism and ensuring that non-financial businesses and professions adhere to AML obligations. For example, Türkiye has strengthened its regulatory framework to enhance due diligence requirements for real estate agents, lawyers, accountants and other professionals who may

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be vulnerable to schemes of money launderers and terrorist financiers.

Türkiye has increased its co-operation with international organisations and foreign FIUs. This includes sharing information and participating in joint investigations to combat cross-border money laundering schemes.



Law and Practice

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Herbert Smith Freehills Kramer (HSF Kramer) was formed in June 2025 through the transformational combination of Herbert Smith Freehills and Kramer Levin, creating a world-leading global law firm. With over 6,000 people including c.2,700 lawyers and spanning 26 offices, HSF Kramer provides comprehensive legal services across every major region of the world. Uniquely positioned to help clients achieve ambitious objectives, HSF Kramer delivers exceptional results in complex transactions and

high-stakes disputes. The dedicated corporate governance advisory team comprises governance specialists with technical expertise who provide practical advice to clients on the full spectrum of governance issues. The team advises listed and privately held companies on the regulatory, reporting and governance standards applicable to them. The firm draws on its wide-ranging experience to advise on legal and regulatory requirements, emerging trends and market best practice.

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1. Introductory

1.1 Forms of Corporate/Business Organisations

Anyone choosing to set up a business in the UK may choose between a broad range of business structures.

The most common type of company in England and Wales is a private company limited by shares. A company limited by shares is one in which, in the event that the company goes into liquidation, the liability of its shareholders is limited to the amount paid or payable when subscribing for those shares (that is, limited liability). Private limited companies are not able to offer shares to the public, meaning they cannot offer shares if they consider those shares might become available to anyone other than those receiving the offer.

Companies that wish to offer securities to the public are most commonly registered as a public company limited by shares. UK legislation also affords limited liability to shareholders in public companies but imposes certain additional restrictions and requirements for the protection of shareholders and creditors. More detail on public companies can be found in **3. Management of the Company**.

Other less frequently used forms of company structure include the following.

- Private unlimited companies, which do not have any limit on the members' liability in the event of the company going into liquidation and being unable to pay its debts.
- Companies limited by guarantee, in which the liability of the subscribers is limited to the amount they have agreed to guarantee. These

are commonly used by non-profit making organisations.

- Partnerships, whereby persons come together to carry on a business with a view to a profit. A general partnership does not have its own legal personality and therefore cannot hold assets other than in the name of the partners. Other forms of partnership in England and Wales are limited partnerships (LP) and limited liability partnerships (LLP). In an LP, one or more partners have limited liability and one or more partners have unlimited liability. An LLP has a separate legal personality and all partners have limited liability.

1.2 Sources of Corporate Governance Requirements

The key sources of law governing the operation of a company incorporated in England and Wales include the following.

- Companies Act 2006 (the “*Companies Act*”) – the UK company law regime is set out in the Companies Act, which is the principal body of legislation governing the formation and management of companies in the UK. The Companies Act has been fully in force since 1 October 2009 and has been amended numerous times since then, most recently by the Economic Crime and Corporate Transparency Act 2023 (ECCTA). The ECCTA became law in October 2023, but its provisions are being commenced in stages.
- Insolvency Act 1986 – this Act contains provisions relating to the insolvency and winding-up of companies.
- Common law – this includes the parts of the law relating to English companies that have no statutory basis but have been established by judges through case law. This body of case law is known as the common law.

- Financial Services and Markets Act 2000 (FSMA) – this Act sets out the UK regime for financial services and securities law. In particular, there are restrictions on offering securities and a requirement for companies to produce a prospectus when they offer their securities to the public (subject to certain exceptions). Again, this Act has been amended since it came into force. In June 2023, the Financial Services and Markets Act 2023 became law. It is being brought into force on a phased basis and, once fully in force, will implement significant reforms to the UK’s financial services regulatory regime, including revoking EU-derived laws relating to financial services and granting enhanced rule-making powers to UK financial services regulators (including the Financial Conduct Authority (FCA), the main regulator of UK listed commercial companies).

In addition, general partnerships, LPs and LLPs are governed by the Partnerships Act 1890, the Limited Partnerships Act 1907 (which is being significantly amended by the ECCTA) and the Limited Liability Partnerships Act 2000, respectively.

A key source of a company’s corporate governance requirements is its articles of association. The articles of association govern the internal affairs of the company and regulate a great range of matters (subject to the requirements of the Companies Act). These include the rights attached to the company’s shares (including voting rights), the powers of the directors, the regulation of shareholders’ and directors’ meetings, the alteration of capital and the transfer of shares.

The key corporate governance codes and principles in the UK include the following.

- The UK Corporate Governance Code (the “*Governance Code*”), which is produced and overseen by the Financial Reporting Council (FRC) (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** for further details on the Governance Code and its application). The current edition was published in January 2024, replacing the 2018 edition with effect from financial years starting on or after 1 January 2025 (except for amendments to one of the reporting provisions which will apply from financial years commencing on or after 1 January 2026). Except where otherwise stated in this chapter, the provisions of the 2024 Governance Code remain substantively the same as previously contained in the 2018 Governance Code.
- The Wates Corporate Governance Principles for Large Private Companies (the “*Wates Principles*”), which sets out corporate governance principles for non-listed companies in the UK. They provide private companies with a framework for complying with reporting requirements imposed on very large UK-incorporated companies to state which corporate governance code, if any, they have applied and how that corporate governance code was applied. The most recent edition was published in December 2018.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

In addition to the requirements of the sources identified in **1.2 Sources of Corporate Governance Requirements**, companies whose shares are publicly traded need to consider the following.

- The Governance Code, which applies to companies listed in the equity shares commercial

companies (ESCC) category, regardless of where they are incorporated (see below on the changes introduced to the UK listing regime in 2024). It sets out principles and provisions relating to board leadership and company purpose; division of responsibilities; composition, succession and evaluation; audit, risk and internal control; and remuneration. The provisions of the Governance Code apply on “*comply-or-explain*” basis that allows for flexibility in the implementation of the provisions by listed companies. However, in practice, the majority of companies to which the Governance Code applies comply with all, or nearly all, of the provisions. The FRC has issued a number of publications which sit alongside the Governance Code:

- (a) the Governance Code guidance, which aims to assist companies implement the 2024 Governance Code;
 - (b) the Stewardship Code, which aims to improve long-term returns to beneficiaries by enhancing the quality and quantity of engagement between investors and companies (last updated in 2025); and
 - (c) the Minimum Standard for audit committees in relation to the external audit process and relations with the external auditor, which was adopted on “*comply-or-explain*” basis for FTSE 350 companies with immediate effect in May 2023 and which is cross-referred to in the 2024 Governance Code.
- The UK Listing Rules, which are issued by the FCA. They set out the requirements for obtaining a listing of securities on the Official List and the mandatory continuing obligations that apply once a company is listed. The listing requirements and continuing obligations which apply to a company depend on which listing category it is admitted to. The UK Listing Rules also govern the requirements

in relation to transactions undertaken by a listed company and the disclosure of relevant information to investors. All companies listed in the ESCC category, regardless of where they are incorporated, are required under the UK Listing Rules to disclose how they have applied the principles of the Governance Code and to confirm that they have complied with the provisions of the Governance Code, or to the extent that they have not complied, explain what has not been complied with and the reasons for this.

- Following a full-scale review of the UK listing regime, in July 2024 the FCA delivered its final rules for a significant restructuring of the UK listing regime which came into force on 29 July 2024. Under the new UK Listing Rules (UKLRs): the premium and standard listing segments were replaced with a single listing segment (the “*equity shares (commercial companies)*” category or “ESCC”), with one set of eligibility requirements and continuing obligations for companies listed in that category (including the requirement outlined above to report against the Governance Code on “*comply-or-explain*” basis). Shareholder votes are no longer required for significant transactions or related-party transactions; and overall the UKLRs have moved from a more rules-based to a more disclosure-based regime.
- The Transparency Rules, which are also issued by the FCA. They require companies to include a corporate governance statement in their annual report, setting out certain prescribed information. They also contain requirements in relation to audit committees (or the body responsible for performing similar functions), setting out the minimum functions the body must carry out and requirements as to the composition of that body. For the most part, the requirements contained in

the Transparency Rules derive from the EU Transparency Directives in force when the UK was an EU member state.

- The UK version of the EU Market Abuse Regulation (UK MAR), which is part of UK law by virtue of the European Union (Withdrawal) Act 2018. UK MAR sets out requirements relating to the disclosure of inside information by listed companies and governs the related offences of insider dealing and unlawful disclosure of inside information. It also restricts when directors may deal in the company's securities and requires directors (and persons closely associated with them) to disclose their share dealings to the relevant company. As noted in **1.2 Sources of Corporate Governance Requirements**, the Financial Services and Markets Act 2023 will, when the relevant sections are brought into force, revoke UK MAR, making way for the FCA to set the rules on the definition and disclosure of inside information. It should be noted though that it is not anticipated that significant changes will be made to the existing regime.
- The AIM Rules, which are published by the London Stock Exchange (LSE), apply to companies with shares admitted to trading on AIM (the market for smaller growing companies in the UK). Additional corporate governance requirements were introduced into the AIM Rules in 2018, requiring AIM companies to state on their website which recognised corporate governance code they apply and to report, on "*comply-or-explain*" basis, against that code. In 2025, the LSE launched a review of AIM which proposes that the AIM Rules should instead set out a simplified list of governance requirements.

A number of institutional investor bodies, including The Investment Association and the Pensions and Lifetime Savings Association, produce

their own corporate governance guidelines that listed companies need to be aware of, and The Chartered Governance Institute UK & Ireland also regularly publishes guidance notes on corporate governance issues.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

The impact companies have on the environment (and vice versa) continues to be one of the dominant topics in corporate governance in the UK (see **2.2 ESG Considerations**).

Many UK companies are now required to make climate-related financial disclosures and following the adoption by the International Sustainability Standards Board (ISSB) of its first two sustainability disclosure standards (SDSs) in June 2023, the UK government is expected to endorse the ISSB SDSs in the first half of 2025 to create UK SDSs.

In addition, the UK Transition Plan Taskforce (TPT) has published a comprehensive framework to help companies develop and report on their net zero transition plans.

Remaining in the ESG sphere, there are also growing concerns among investors about "*greenwashing*", which is becoming an increasing focus area for regulators.

Diversity and inclusion at board and senior management levels are also issues that the largest companies in the UK are being requested to focus on, in order to seek to improve how reflective these bodies are of society at large (see **4.3 Board Composition Requirements/Recommendations**).

Executive compensation, and in particular pay gaps between executive and employee pay, is another major focus area for shareholders and other stakeholders (see **4.10 Approvals and Restrictions Concerning Payments to Directors/Officers** and **4.11 Disclosure of Payments to Directors/Officers**).

2.2 ESG Considerations

Environmental, social and governance (ESG) issues remain an area of significant focus for regulators, investors and other stakeholders in the UK.

Listed companies are required to include a statement in their annual financial report which sets out whether the report contains disclosures consistent with the recommendations and recommended disclosures of the Task Force on Climate-related Financial Disclosures (TCFD) and to explain why, if they do not. Separately, the Companies Act places requirements on certain publicly quoted companies and large private companies to incorporate TCFD-aligned climate disclosures in the non-financial and sustainability information statement which forms part of the strategic report in their annual report and accounts (see **6.1 Financial Reporting** for more information on the strategic report).

As noted above, the ISSB issued two SDSs in the summer of 2023, and the UK government is expected to endorse these to create UK SDSs during the first half of 2025. The FCA will then consider the application of UK SDSs and the TPT's framework to companies listed in the UK. For listed companies, the new ISSB-based regime is expected to apply in place of the TCFD-based regime and it is anticipated that disclosure of transition plans will become mandatory.

These climate-related disclosures supplement the existing requirements for certain listed companies to include prescribed non-financial information, including on environmental, workforce and social matters and respect for human rights, in their annual report (see **6.1 Financial Reporting** for more information).

Companies subject to the Governance Code or the Wates Principles are also required to report on certain non-financial aspects of their business and stakeholders.

There are a number of other reporting requirements for companies relating to ESG issues. Companies that meet certain thresholds must publish statements explaining:

- how their directors have performed their duty under Section 172 of the Companies Act to have regard to the various stakeholder factors listed in Section 172 (1) (including employees, customers and suppliers, the community and environment);
- how their directors have engaged with employees and had regard to UK employee interests, and the effect of that regard, including on the principal decisions taken by the company; and
- how their directors have had regard to the need to foster the company's business relationships with suppliers, customers and others, and the effect of that regard, including on the principal decisions taken by the company.

For a number of years, commercial organisations operating in the UK that meet certain size requirements have been required under the Modern Slavery Act 2015 to publish a statement discussing the steps they have taken to ensure that slavery and human trafficking is not taking place in their business or supply chain.

The UK government has indicated that it intends to strengthen this reporting obligation, including by mandating certain content requirements and requiring publication on a government-sponsored website, though the timing for any changes is not known. In the interim, the UK government has published updated guidance for in-scope entities on the requirements of the Modern Slavery Act.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management

The principal bodies and functions involved in the governance and management of a company in the UK are set out below.

- The board of directors – as discussed in **4.3 Board Composition Requirements/Recommendations**, a company is required to appoint directors. The articles of association of the company will typically delegate management of the company to the directors, enabling them to execute all the powers of the company. The composition and activities of a board of directors will vary depending on the company's circumstances. Publicly listed company boards will include a number of non-executive directors in accordance with the provisions of the Governance Code. For companies which are not listed, the board is usually comprised of executive directors who are involved in the day-to-day management of the business. An unlisted company may appoint non-executive directors to the board, and the Wates Principles encourage large private companies to consider this.
- The company secretary – it is a requirement under the Companies Act for a public company to have a company secretary. Private

companies are not required to have a company secretary. The role of the company secretary is to support the board and advise on corporate governance issues.

- The executive management team – the responsibility of the executive team is to implement the board's decisions and policies, and deal with the day-to-day management of the company. In unlisted companies, the executive team will often comprise of the same individuals as the board of directors. In a publicly listed company, the CEO and CFO will usually be directors of the company, with the remaining members of the executive team forming/sitting on an executive committee or equivalent.
- Shareholders – the shareholders are the owners of the company, and those who hold the board of directors to account. The articles of association and the Companies Act provide that a number of decisions are reserved for shareholders (see **3.2 Decisions Made by Particular Bodies**).

3.2 Decisions Made by Particular Bodies

Decision-making by a company is generally delegated to the board of directors in the company's articles of association (although there are some decisions that are reserved for the shareholders). The key decisions made at each level of the management of a company are as follows.

- The board of directors – most decisions are made by the board of directors and will typically relate to the strategy and general management of the company.
- The management team – where the management team is different to the board of directors, it will make decisions on the day-to-day business of the company pursuant to powers delegated by the board of directors.

- Shareholders – under the Companies Act, there are a number of decisions (eg, amending the articles of association and certain share capital matters) that are reserved for shareholders and can only be passed by shareholder resolution. In some cases, these decisions can be delegated to the board of directors under a company's articles of association.

3.3 Decision-Making Processes

The board of directors, management team and shareholders make decisions in the following ways.

- The board of directors – decisions by the board are taken in the form of board resolutions and are typically taken at a board meeting. The procedures for board meetings and the voting requirements for board resolutions are set out in the company's articles of association. Resolutions are typically passed by a simple majority. Board resolutions may also take the form of written resolutions, meaning a board meeting does not have to be physically convened. The articles of the company may also permit directors to meet virtually, using videoconferencing or similar communication tools. When making decisions, the directors must have regard to their general duties under the Companies Act (see **4.6 Legal Duties of Directors/Officers**).
- The management team – the management team implements decisions made by the board but acts through delegated authorities from the board. As such, decisions must be made within the terms of the delegation.
- Shareholders – decisions by shareholders are taken in the form of shareholder resolutions at a general meeting (or for private companies only, they may be taken by written resolution, in which case a physical meeting will not

be required). In order to convene a general meeting to pass a shareholder resolution, a company must provide shareholders with notice of the meeting, including information about the issues that are to be resolved. The Companies Act stipulates the approval threshold for each type of shareholder decision to be passed, which is typically either a simple majority (required to pass an ordinary resolution) or a majority of not less than 75% (required to pass a special resolution). Most shareholder resolutions can be passed by an ordinary resolution though some, such as an amendment to the articles of association or a disapplication of pre-emption rights on an allotment of shares, require a special resolution. Public companies, but not private companies, are required under the Companies Act to hold an annual general meeting of shareholders (AGM). Standard business for an AGM includes the re-election of directors, appointment of an auditor and authorisation of certain matters in relation to a company's share capital.

4. Directors and Officers

4.1 Board Structure Requirements in Law

In terms of board structure, companies have a single-tier, unitary board. Executive and non-executive directors are both members of the board, in contrast to other jurisdictions where non-executive directors sit on a separate supervisory body.

Under the Companies Act, private companies must have at least one director, and public companies at least two directors and a company secretary. For all companies, directors must be over 16 years of age.

Once the relevant provisions of the ECCTA are brought into force, all new and existing company directors will need to have their identity verified and it will be an offence for an unverified person to act as a director of a company. From April 2025, individuals have been able to voluntarily verify their identity, ahead of identity verification becoming mandatory for all directors on incorporation and appointment in autumn 2025 (with a 12-month transition period for existing directors).

Requirements Under the Governance Code

The Governance Code provides that at least half the board, excluding the chair, should be comprised of independent non-executive directors. The Governance Code also provides that companies should form three committees: a nomination committee, a remuneration committee and an audit committee. The nomination committee should lead the process for making and recommending appointments to the board. The main role of the audit committee is to monitor the integrity of the company's financial statements and review the company's internal controls. The remuneration committee should have responsibility for determining the policy for executive director remuneration and setting remuneration for the chair, executive directors and senior management. The remuneration and audit committees should be comprised entirely of independent non-executive directors and the nomination committee should have a majority of independent non-executive directors.

4.2 Roles of Board Members

Directors can be executive (with a service contract) or non-executive. The board of directors will typically comprise the following.

- Chair of the board – their role is to chair board meetings and take on a leadership

role to ensure the effectiveness of the board. The Governance Code states that the chair should not be the same person as the CEO, to ensure independence.

- Non-executive directors – the Governance Code provides that at least half the board, excluding the chair, should be independent as assessed by reference to various criteria set out therein. The Governance Code says that the role of non-executive directors is to challenge and advise the board on the company's strategy and policies. The Wates Principles state that privately held companies should have due regard to the benefits independent non-executive directors can bring.
- Senior independent director (SID) – the Governance Code provides that the board should appoint one of the independent non-executive directors to be the SID, who should provide a sounding board for the chair and serve as an intermediary for the other directors and shareholders.
- Executive directors – executive directors on the board may include a CEO, CFO and chief operating officer (COO). There are no specific legal requirements regarding which executive directors a company should appoint. The number and type of executive directors appointed will depend on the business needs of the company. The role of the executive directors is to implement the decisions made by the whole board and to discharge overall managerial responsibilities. For example, a CEO is typically responsible for the overall management of the company, while a CFO is responsible for the company's accounts and finances, and a COO is responsible for the overall operations and administration of the company. The executive directors will be supported in their role by members of the executive team, who are not part of the board.

4.3 Board Composition Requirements/Recommendations

Subject to the provisions of the Companies Act, the articles of association may prescribe a maximum or minimum number of directors. Subject to certain requirements, corporate directors are currently permitted, but at least one director must be an individual. However, it is anticipated that, along with other changes in relation to directors being introduced by the ECCTA, a prohibition on the use of corporate directors (except in limited circumstances) will be brought into force in the near future.

There are no formal qualifications required under the Companies Act in order to be appointed as a director. The Governance Code provides that the directors have appropriate skills, experience, independence and knowledge of the business to discharge their responsibilities properly and effectively. The Governance Code also contains provisions on diversity and inclusion with regard to both board appointments and succession plans.

There has been a focus on board diversity for a number of years in the UK and various initiatives have been launched in this area. These include the FTSE Women Leaders Review, which recommends that by the end of 2025, for FTSE 350 companies, a minimum of 40% of both the board of directors and leadership team should be female. In addition, the Parker Review set a target for listed companies to have at least one director from an ethnic minority background. For FTSE 100 companies the target date set was the end of 2021; for FTSE 250 companies this target should have been met by the end of 2024. The Parker Review also requested FTSE 350 companies to set themselves a target for the percentage of their senior management which self-identifies as being from an ethnic minority group,

which they should meet by December 2027. Aligning with these reviews, under the UKLRs, listed companies are required to make certain disclosures in relation to gender and ethnic diversity at board and executive management level, including reporting on “*comply-or-explain*” basis against diversity targets for the representation of women and minority ethnic groups on the board and providing numerical disclosures on the diversity of the board and executive management. Both the FTSE Women Leaders Review and the Parker Review have extended their recommendations regarding board diversity to the top 50 private companies in the UK (as determined by sales).

4.4 Appointment and Removal of Directors/Officers

The Companies Act sets out the requirements for appointing directors upon incorporation of a company but is silent on subsequent appointments. Therefore, the process will be set out in the company’s articles of association, which usually stipulate that directors can be appointed by a decision of the board of directors or by shareholders, in each case by simple majority.

In line with the provisions of the Governance Code, listed companies typically have a nomination committee that has responsibility for recommending board appointments. Under the Governance Code, all directors should stand for re-election annually at the company’s AGM, regardless of the size of the company (see 1.3 **Corporate Governance Requirements for Companies With Publicly Traded Shares** for details of the application of the Governance Code).

There are a number of ways a director can be removed from office. The Companies Act provides that a director may be removed by ordinary resolution (before the expiration of the director’s

term). If a director is to be removed before the expiration of their term, the Companies Act sets out a number of protections that must be complied with, including that the ordinary resolution cannot be a written resolution and that the director has the right to be heard by the shareholders at the general meeting. In addition, a company's articles of association typically set out grounds for removal.

4.5 Rules/Requirements Concerning Independence of Directors

Independence

There are no requirements at law regarding independence of directors. However, the Governance Code provides that at least half the members of the board should comprise independent non-executive directors, determined in accordance with the Governance Code (see **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** for details of the application of the Governance Code). Circumstances which the Governance Code considers are likely to impair, or appear to impair, non-executive directors' independence include whether they:

- have been employees of the company or group within the last five years;
- have had a material relationship with the company in the last three years;
- have close family ties with any of the company's advisers, directors or senior employees;
- have served on the board of the company for more than nine years; or
- represent a significant shareholding.

However, a company may, notwithstanding the existence of these circumstances, determine a director to be independent. If they do so, this should be explained in the company's annual report.

Conflicts of Interest

Under the Companies Act, directors have a duty to avoid situations in which they have, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company. The duty is stated to apply, in particular, to the exploitation of any property, information or opportunity. A director will therefore need to consider carefully whether an opportunity rightfully belongs to the company before exploiting it personally.

There are a number of exceptions to this duty, including where the matter has been authorised by the company's directors, where the company has given authority to the directors for something to be done or where the articles of association contain a provision for dealing with conflicts and the directors are acting in accordance with that provision.

Directors have three related duties, including the duty not to accept benefits from third parties, the duty to declare any interest in a proposed transaction and the duty to declare an interest in an existing transaction (see **4.6 Legal Duties of Directors/Officers**). These interests would typically be declared at the board meeting authorising the transaction.

4.6 Legal Duties of Directors/Officers

The rules governing directors' duties are set out in the Companies Act.

The Companies Act includes a statutory statement of the duties a director owes to the company. The statutory directors' duties are:

- to act within the powers conferred by the company's constitution;
- to promote the success of the company for the benefit of the members as a whole;

- to exercise independent judgment;
- to exercise reasonable care, skill and diligence;
- to avoid conflicts of interest;
- not to accept benefits from third parties; and
- to disclose an interest in a proposed transaction with the company.

The duties apply to all the directors of a company. However, the statutory statement of duties does not cover all the obligations of a director. Other obligations are contained throughout the Companies Act, such as the duty to deliver accounts and the obligation to disclose an interest in an existing transaction with the company. There are also obligations contained in other statutes; for example, the Insolvency Act 1986. In addition, directors have a general fiduciary duty to their shareholders that arises from the relationship of trust and confidence between them and their shareholders.

4.7 Responsibility/Accountability of Directors

The directors' statutory duties as set out in the Companies Act are owed directly to the company (not to any individual shareholder(s) or to any stakeholder(s)). However, embedded within them is a requirement to have regard to the interests of a number of stakeholders. The duty to promote the success of the company requires directors to have regard to the interests of its employees, community and the environment, and to foster the company's relationships with suppliers, customers and others when considering this duty.

In addition, the directors owe a fiduciary duty under the common law to shareholders to provide them with information that is sufficient, clear and not misleading, to enable them to make an informed decision as to how to vote at a share-

holder meeting. Directors also have a common law duty to consider the interests of the company's creditors when a company is facing actual, imminent or probable insolvency (ie, the "*creditor duty*"), which was affirmed by the Supreme Court in a 2022 court judgment.

4.8 Consequences and Enforcement of Breach of Directors' Duties

As a general rule, a company is the only person able to bring a claim against one of its directors for breach of duty, since the duty is owed by the directors to the company itself. This means that a shareholder (acting on their own behalf) cannot bring an action against a director for breach of duty. This results in practical difficulties, in so far as the board is unlikely to approve the company bringing an action against one of its own for breach of duty. To mitigate this, the Companies Act contains a statutory procedure pursuant to which a shareholder may, in certain circumstances, bring a derivative claim on behalf of the company. Further detail on such actions is set out in 5.4 Shareholder Claims.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In addition to liability relating to breaches of duty, directors may also be liable for breaches of statutory provisions within the Companies Act, such as those relating to unlawful distributions or unlawful directors' remuneration payments. In certain circumstances, directors may also be subject to criminal penalties, particularly in relation to health, safety and environmental matters; competition and anti-competitive behaviour; and bribery, corruption and fraud.

Directors can, to an extent, protect themselves from the liabilities arising from their role; however, there are some limitations on public policy grounds. A company may generally indemnify

directors against liability incurred towards a third party in the performance of their role. However, companies may not indemnify their directors for breaches of duties or negligence. Similarly, there are limitations to the extent to which a company can indemnify directors in circumstances where criminal proceedings are being brought against them.

A company may also purchase D&O insurance for directors.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

At law, approval by shareholders is required for any director's service contract for which the guaranteed term is longer than two years. Failure to obtain approval makes the relevant contractual provision void and allows the company to terminate the service contract at any time by giving reasonable notice.

A quoted company (that is, a company whose equity share capital is listed on the Official List in the UK, a company officially listed in an EEA state or admitted to dealing on NASDAQ or the NYSE) may not make any remuneration payment to a director or former director unless that payment is in accordance with its latest remuneration policy approved by shareholders (or the payment has been separately approved by shareholders). The directors' remuneration policy is a binding policy and must be approved by an ordinary resolution of shareholders at least once every three years. In addition, shareholders are required to vote annually on a statement disclosing the directors' remuneration for the previous year. This vote is indicative and does not have the effect of clawing back any payment that has already been made. However, if the directors' remuneration report is not approved

by shareholders, the company is required to table a new remuneration policy the following year. For financial years beginning on or after 11 May 2025, these requirements no longer also apply to non-quoted traded companies, that is, companies which do not fall within the definition of quoted company but with voting shares admitted to trading on a UK regulated market or an EU regulated market.

4.11 Disclosure of Payments to Directors/Officers

The Governance Code also places additional reporting requirements on a company's remuneration committee in relation to the pay of directors and senior managers. The remuneration committee is required to provide a full description of its work in the annual report, including an explanation of the strategic rationale for remuneration decisions, the application of discretion to remuneration outcomes and details of shareholder and workforce engagement on the remuneration policy.

A quoted company must also publish the pay difference between its CEO and its average UK employee.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

A shareholder's relationship with the company in which they hold shares is a contractual one. Under the Companies Act, the articles of association bind the company and its members to the same extent as if they were covenants on the part of the company and each member to observe the provisions. The articles of association therefore constitute a form of contract between the company and its shareholders,

and between the shareholders themselves. The shares held by the members give a right of participation in the company on the terms of the articles of association.

A shareholder does not have a proprietary interest in the underlying assets of a company. Shareholders are entitled in proportion to their respective shareholdings to a share of the distributed profits of the company and, on a winding-up, to the surplus assets of the company after the company's creditors have been repaid in full. Shareholders are not liable for the acts of the company, except in very limited circumstances when the corporate veil can be pierced, where a company's limited liability status is set aside and a shareholder is liable for the company's acts.

5.2 Role of Shareholders in Company Management

The articles of association usually delegate to the directors the exercise of the powers of the company, save for those powers that are required by the articles or the Companies Act to be exercised by the shareholders in a general meeting or by shareholder resolution. Therefore, it is rare for shareholders in their capacity as such to have involvement in the day-to-day running of the company. Shareholders in joint venture companies may agree contractually that certain actions will not be taken by the company unless agreed by a particular number, or majority, of shareholders.

If desired, shareholders can direct the management of a company to take, or refrain from taking, certain actions in the business by directing the directors to call a general meeting. Shareholders must hold more than 5% of the voting rights to make this request and must explain the general nature of the issues they wish to raise at the meeting. Directors will not be required to table

a resolution if it is defamatory, frivolous or vexatious, or if it would not be effective if passed.

5.3 Shareholder Meetings

A public company is required to hold an AGM every year within six months of its financial year-end. There is no statutory requirement for a private company to hold an AGM (unless they are traded companies) but there may be an express requirement to hold one in the company's articles of association. For public companies, 21 clear days' notice of the AGM is required, unless all who are entitled to attend and vote consent to shorter notice being given.

Any shareholder meeting other than an AGM is a general meeting. The minimum statutory notice period required for a general meeting of a private company (which is not a traded company) is 14 clear days. For public companies, the minimum statutory notice period for general meetings other than AGMs is 14 clear days, however it is 21 clear days for public companies which are traded companies. Traded companies can reduce the minimum notice period for these meetings to 14 clear days if (i) shareholders have passed an annual resolution to shorten the notice period to 14 clear days, and (ii) the company allows shareholders to appoint a proxy by electronic means via a website.

Shareholders holding 90% (in the case of private companies) or 95% (in the case of public companies) of the nominal value of shares giving a right to attend and vote may agree to shorter notice of general meetings. The articles of association may specify a longer notice period (but the articles of association cannot specify a shorter period).

Until recently, shareholder meetings were almost exclusively physical meetings and there were

very few examples of virtual-only meetings (that is, a shareholder meeting held exclusively through the use of online technology, with no physical meeting) or hybrid shareholder meetings (that is, a physical shareholder meeting with the option for electronic participation through the use of online technology).

Whilst certain relaxations were accepted during the COVID-19 pandemic, these relaxations no longer apply and, in the absence of such relaxations, there are questions as to the validity of virtual-only shareholder meetings under English law. Investor bodies, such as the Investment Association, have expressed concerns over virtual-only meetings. These bodies are generally more amenable to hybrid meetings, though there are practical issues with hybrid meetings which limit their popularity with companies. In all instances, companies are required to comply with the provisions of their articles of association in relation to proceedings at shareholder meetings. Many companies have therefore amended their articles of association in order to facilitate the holding of hybrid shareholder meetings should the need for such flexibility arise again in the future. In October 2024, the Department for Business and Trade (DBT) announced that it will carry out a review of shareholder communications in light of emerging technologies and to clarify the legal framework surrounding virtual AGMs.

5.4 Shareholder Claims

As noted in 4.8 **Consequences and Enforcement of Breach of Directors' Duties**, as a general rule, a company is the right person to bring a claim against one of its directors for breach of duty, since the duty is owed to the company. However, the Companies Act contains a statutory procedure under which a shareholder may bring a derivative claim – that is, proceedings

on behalf of a company – against a director for negligence, default, breach of duty or breach of trust.

The factors that the court will look at when deciding whether to allow a derivative claim include whether a director who is acting to promote the success of the company would proceed with it, whether the relevant act or omission was previously authorised by the company, whether the breach has been ratified, and the views of independent shareholders.

In addition, shareholders can apply to the court for protection against unfair prejudice if they believe the company's affairs are being or have been conducted in a manner that is unfairly prejudicial to the interests of its members or a group of its members.

Claims against the company may also arise if a publicly traded company does not behave properly in relation to the treatment of the release of information to the market. In particular, under Section 90A of the FSMA, a company may be liable to pay compensation to a person who acquires, continues to hold or disposes of the company's securities in reliance on information disclosed by the company using recognised means and who suffers loss in respect of the securities as a result of either any untrue or misleading statement in that published information, or the omission from that published information of any information required to be included in it. The company is only liable, however, if a person discharging managerial responsibilities knew that the statement was untrue or misleading, or was reckless as to whether it was, or knew the omission was a dishonest concealment of a material fact.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Any shareholder whose interest in the voting rights of a publicly traded company reaches, exceeds or falls below 3%, 4%, 5% and each 1% threshold thereafter must disclose this to the company, which must notify the market. Where the company is listed on the LSE's Main Market, the shareholder must also send a notification to the FCA.

The Takeover Code (which governs takeovers and mergers in the UK) requires that for any public listed company, if any person, or group of persons acting in concert, acquires 30% or more of the company's voting rights, they will trigger an obligation to make a general takeover bid to acquire the remainder of the shares.

All companies incorporated in the UK are required to maintain a register of persons with significant control (PSCs), which is effectively a register of beneficial ownership, and register the details of its PSCs with Companies House. It is worth noting that the ECCTA will introduce identity verification requirements for all existing and new PSCs (expected to commence from autumn 2025, see **4.1 Board Structure**), with a view to improving transparency around ownership and control in UK corporate structures. Disclosure obligations have also been extended in relation to the beneficial ownership of overseas companies which own, or wish to own, land or property in the UK and which are now required to be entered on a register held by Companies House.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

Companies are required to publish an annual report and accounts for each financial year, unless an exemption applies. A public company must do so within six months of the end of its financial year, whereas a private company must do so within nine months. The Companies Act sets out the content requirements of the annual report and accounts, which is supplemented by various regulations, including The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended). Generally, the Companies Act requires the annual report and accounts to comprise a directors' report, financial statements and, for companies above a certain size threshold, a strategic report. Quoted companies are also required to include a directors' remuneration report. Listed companies also include a corporate governance statement discussing their corporate governance arrangements.

The purpose of the strategic report is to inform members of the company and help them assess how the directors have performed their duty under Section 172 (duty to promote the success of the company). It must contain a fair review of the company's business and a description of the principal risks and uncertainties facing the company. It must also contain an analysis of the development and performance of the company's business during the financial year and the position of the company's business at the end of the year, consistent with the size and complexity of the business. Certain companies must also include in the report a statement of how the directors applied the principles of Section 172 during the financial year, information on their environmental impact, workforce gen-

der diversity statistics, and board consideration of employee and supplier matters. The strategic report may also contain key performance indicators on various financial and non-financial matters. Companies which are “*public interest entities*” (that is, companies whose transferable securities are admitted to trading on a regulated market, insurers and credit institutions) with more than 500 employees, are required to include prescribed non-financial information in their strategic report. The required information includes:

- disclosures in relation to anti-corruption and anti-bribery matters, environmental matters, employees, social matters and respect for human rights;
- a description of the company’s policies in relation to the non-financial matters;
- the principal risks relating to the non-financial matters arising in connection with the company’s operations; and
- TCFD-aligned climate-related financial disclosures.

The climate-related financial disclosure requirements also apply to all companies with a turnover of more than GBP500 million and over 500 employees. As noted above (**2.2 ESG Considerations**), it is anticipated that the climate-related financial disclosures will in the future be aligned to the ISSB disclosure standards, rather than to the TCFD regime.

The directors’ report is now, in practice, a repository for a number of miscellaneous statutory disclosures, including in relation to the directors, company constitution, share capital and political donations.

See **4.11 Disclosure of Payments to Directors/Officers** for discussion of the content require-

ments of the directors’ remuneration report; and see **6.2 Disclosure of Corporate Governance Arrangements** for discussion of the content requirements of the corporate governance statement.

The UK government is carrying out a review of non-financial reporting requirements and has already made a number of changes to the disclosures required in the directors’ report and the directors’ remuneration report. Further changes are expected to be consulted on during 2025.

For listed companies, the content requirements set out above are supplemented by the provisions contained in the Transparency Rules. In particular, these provide that the annual report must include consolidated audited accounts, a management report and a responsibility statement. The Transparency Rules require a company to publish an annual report as soon as possible and in any event within four months of the end of each financial year. The Transparency Rules also require listed companies to produce a half-yearly report within three months of the half-year end comprising a condensed set of financial statements, an interim management report and responsibility statements. The Transparency Rules also set out the requirements in respect of the format for annual reports, which include that the annual report must be prepared and published in structured electronic format.

6.2 Disclosure of Corporate Governance Arrangements

The Governance Code does not have the force of law but, as noted in **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares**, pursuant to the Listing Rules, companies listed in the ESCC category are required to report annually on how they have applied the principles of the Governance Code

in a manner that would enable shareholders to evaluate that application and state whether they have complied with the provisions of the Governance Code, and if not, explain the reasons for this.

The Governance Code also sets out certain information that should be included in the corporate governance statement contained in the annual report. This includes discussion of matters such as board composition, the remuneration of directors and the relationship between a company and its auditor.

Private companies over a certain size are required to include in their annual report a statement on the company's governance arrangements.

6.3 Companies Registry Filings

A company must notify Companies House (the registrar of companies) as and when there are any changes to its particulars, such as the registered office, directors or changes in share capital. In addition, all special resolutions must be filed at Companies House within 15 days of being passed, and the Companies Act specifies certain ordinary resolutions that are also required to be filed at Companies House (eg, an ordinary resolution authorising directors to allot shares). All documents filed with Companies House are publicly available for free online.

A company must also file certain information with Companies House, on an annual basis. This includes the annual report and accounts. The annual filing requirements also include a confirmation statement confirming information in respect of its shareholders, directors and PSCs and confirming that the intended future activities of the company are lawful. The first confirmation statement filed after the identity verification requirements come into force will also need to

confirm that the company has complied with the identity verification requirements for existing directors (see 4.1 Board Structure).

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

A company is required to appoint an external auditor when preparing its annual accounts unless it is subject to an exemption. Small and dormant companies are exempt from audit unless a sufficient number of members require an audit. For financial years beginning on or after 6 April 2025, a company will be classed as small if it is not exempt and meets two of the following three thresholds:

- it must have an annual turnover of not more than GBP15 million;
- it must have a balance sheet total of not more than GBP7.5 million; or
- its average number of employees must be not more than 50.

Directors are responsible for the preparation of the company accounts in accordance with all relevant law and regulations. Auditors report on whether the accounts meet the requirements as asserted by the directors, but this does not relieve the directors of their responsibilities.

There are additional requirements that govern the relationship between companies which are “*public interest entities*” (that is, companies whose transferable securities are admitted to trading on a regulated market, insurers and credit institutions) and their auditors, such as the mandatory rotation of auditors after a maximum of 20 years, the requirement to run a tender process of audit services and the auditor being

prevented from undertaking certain non-audit services for the company.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The Governance Code places requirements on companies listed in the ESCC category to confirm within their annual report that they have carried out a robust assessment of the company's emerging and principal risks. Directors are also required to:

- explain how risks are being managed or mitigated;
- explain how they have assessed the prospects of the company; and
- state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of the board's assessment.

In addition, to assess the company's financial risks and controls, listed companies are required to appoint an audit committee of non-executive directors, whose role is to ensure that shareholder interests are properly protected in relation to financial reporting.



Law and Practice

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Sullivan & Cromwell LLP has a record of success and client service, which has been perfected over 140 years and made the firm one of the models for the modern practice of law. Today, it is considered one of the leaders in each of its core practice areas and geographic markets. S&C advises a diverse range of clients on

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1. Introductory

1.1 Forms of Corporate/Business Organisations

In the USA, there are three principal forms of business organisations: corporations, partnerships and limited liability companies.

Corporations

Most public companies are corporations. A corporation is an entity owned by stockholders, managed by a board of directors and established by the filing of a certificate of incorporation or similar document with the secretary of state of a US state. Corporations can be privately held or publicly traded on a stock exchange, with public corporations having more stockholders. The board of directors typically delegates day-to-day management of the corporation to the corporation's executive officers but exercises oversight over such management. A corporation is liable for the obligations of its business, but its stockholders are generally not held liable for such obligations.

State law typically requires a corporation to hold board meetings and annual stockholder meetings. Although corporations have comparatively less governance flexibility and are subject to certain other disadvantages compared to oth-

er entity forms (including entity-level taxation), large and widely held public companies are usually organised as corporations, as they are recognised as the traditional corporate form and tend to be the preferred investment vehicle for investors.

Certain states provide for other forms of for-profit corporations, such as public benefit corporations and statutory close corporations. A public benefit corporation is organised for the purpose of a public benefit rather than for the primary purpose of enhancing stockholder value. Statutory close corporations (which are required to have less than a specified number of stockholders) are typically subject to fewer governance formalities than ordinary corporations.

Partnerships

There are two forms of partnerships: general partnerships and limited partnerships.

A general partnership is an entity in which two or more persons carry on the entity's business. In a general partnership, each partner has the authority to undertake transactions, execute contracts and incur liabilities on behalf of the partnership, and is also personally responsible for the obligations of the partnership. State law does not require formal documentation in order

to establish a general partnership, however, sophisticated parties often enter into a partnership agreement to specify the rights and obligations of the partners. Certain states provide for a limited liability partnership, which is a special type of general partnership. In a limited liability partnership, each partner is only personally responsible for liabilities arising from their own conduct on behalf of the partnership.

A limited partnership is an entity with two classes of partners: general partners and limited partners. A limited partnership is formally established by the filing of a certificate of limited partnership or similar filing with the secretary of state. The general partner manages the day-to-day affairs of the limited partnership and is personally liable for the partnership's obligations. Limited partners are mostly passive investors, and their liability is capped at their investment as long as they do not exert active control over the limited partnership. State law governing limited partnerships is generally flexible, and the governance of limited partnerships can be customised to the preferences of the contracting parties.

Limited Liability Companies

A limited liability company (LLC) is an entity formed by one or more members by filing a certificate of formation or similar document with the secretary of state. Similar to a corporation, members of an LLC benefit from limited liability. As with a limited partnership, state law generally permits the governance formalities of an LLC to be customised to the parties' preferences in an operating agreement.

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance requirements for US companies are state statutory and common law, the entity's organisational

documents, federal securities laws and regulations, the stock exchange regulations and influential (but non-binding) non-legal guidelines, such as proxy advisory firms' guidelines and institutional investor voting policies.

State Law

State law is derived from a state's corporations code and related case law. The specific state's law that applies to an entity generally depends on its chosen state of incorporation. In the USA, the most common state of incorporation for public companies is Delaware, where the Delaware General Corporation Law (DGCL) governs the affairs of Delaware corporations. The DGCL consists of a set of default and mandatory rules. Incorporators may generally opt out of the DGCL's default rules in a corporation's organisational documents, but a corporation is required to adhere to the DGCL's mandatory rules.

The expertise of the Delaware judiciary and its active role in the development of corporate case law have generally been perceived as an advantage for Delaware corporations. Entity forms other than corporations are governed by other statutes and case law under state law.

Organisational Documents

An entity's organisational documents set forth its governance rules, including any modifications the entity adopts to the default provisions under state law. The nature of these documents generally depends on the corporate form and state of incorporation of the entity. For example, a Delaware corporation is governed by a certificate of incorporation and by-laws and, in certain circumstances, a stockholders' agreement. A general partnership and limited partnership are governed by a partnership agreement, and an LLC is governed by an operating agreement.

Federal Securities Laws

For public companies, the Securities Act of 1933 and the Securities Exchange Act of 1934 (Exchange Act), as amended by the Sarbanes-Oxley Act of 2002 (SOX) and the Dodd-Frank Act of 2010 (Dodd-Frank), establish certain rules and disclosure requirements pertaining to corporate governance. Historically, the federal securities laws indirectly regulated the corporate governance of public companies through a disclosure regime. However, SOX and Dodd-Frank added substantive corporate governance rules, such as independence requirements for audit committee members.

Proxy Advisory Firms

Proxy advisory firms, such as Institutional Shareholder Services (ISS) and Glass Lewis & Co (Glass Lewis), issue guidelines to advise stockholders of public companies on how to vote their shares on corporate governance matters. Passive institutional investors often vote on corporate governance matters in accordance with such guidelines, as well as their investors' published voting policies. Given the trend towards shares being held passively, these guidelines and policies play a significant role in the governance of public companies.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

The USA has two primary national stock exchanges: the New York Stock Exchange (NYSE) and the Nasdaq Stock Market (Nasdaq). US companies with publicly traded shares are generally required to follow the corporate governance rules and disclosure requirements set forth in the applicable stock exchange rules and the federal securities laws. These requirements are mandatory, although the stock exchanges provide exemptions for certain companies, such

as those with a controlling stockholder, limited partnerships, companies in bankruptcy, smaller reporting companies, registered investment companies, and foreign private issuers.

Director Independence

The NYSE and Nasdaq require a majority of a listed company's board of directors to be composed of independent directors, and boards are required to make the affirmative determination as to whether each director qualifies as independent under the applicable exchange's definition of independence. The NYSE definition of independence requires that a director has no material relationship with the company. Nasdaq's definition of independence turns on whether the director has a relationship that would interfere with the exercise of the independent judgement of the director in carrying out their responsibilities. Although these determinations generally require an assessment of all relevant facts and circumstances, each of the stock exchanges also includes bright-line tests that, if satisfied, disqualify a director from being independent.

These tests relate to:

- whether the director or an immediate family member has been employed by or received compensation above a certain threshold from the listed company;
- whether the director or an immediate family member is employed by another company that makes or receives payments above a certain threshold from the listed company;
- whether the director or an immediate family member is employed by the listed company's auditor; and
- whether the director or an immediate family member is employed by another company where any of the listed company's executive

officers serve on the other company's compensation committee.

Executive Sessions

The NYSE and Nasdaq require independent directors to hold executive sessions once and twice a year, respectively, without the presence of management. The NYSE requires disclosure of the name of the presiding director at each executive session or the method by which that presiding director was selected. The NYSE also requires a listed company to disclose the method for interested parties (not just stockholders) to communicate with the presiding director of the executive session or the independent directors as a group.

Composition of Board Committees

The stock exchanges generally require public companies to have three board committees: audit, compensation and nominating and corporate governance. Stock exchange rules and the federal securities laws include extensive rules regarding the composition and responsibilities of these three committees. Boards of public companies typically have other committees in addition to the three mandatory committees.

Audit Committee

NYSE- and Nasdaq-listed companies must have an audit committee with at least three members who are independent under the stock exchange rules and Rule 10A-3 under the Exchange Act. In order to be considered independent under Rule 10A-3 under the Exchange Act, audit committee members must not accept any consulting, advisory or other compensatory fee from the listed company or its subsidiaries, or be affiliated with the listed company or its subsidiaries. In addition, Nasdaq precludes a director who participated in the preparation of the financial statements of the company or its subsidiaries

in the past three years from serving as an audit committee member.

The NYSE and Nasdaq require all audit committee members to have a certain level of financial literacy and one member to have a certain level of financial expertise. The NYSE also restricts service on multiple audit committees, providing that if a director serves on the audit committee of more than three public companies, the board must determine that such service would not impair the director's ability to serve effectively on the listed company's audit committee, and the board must disclose that determination publicly.

In addition to imposing requirements for audit committee members, stock exchange rules and the federal securities laws also specify certain powers and responsibilities that audit committees must have, including:

- appointing and overseeing outside auditors;
- establishing procedures for the receipt and treatment of complaints regarding accounting matters; and
- authority to engage and pay independent advisers.

The NYSE mandates additional responsibilities of audit committees that are not otherwise required by Nasdaq rules, including:

- annually reviewing the report of the listed company's independent auditor relating to the auditor's quality control procedures, any quality control issues identified and measures taken to address such issues;
- reviewing and discussing the listed company's annual and quarterly financial statements with management and the independent auditor;

- discussing the listed company's earnings press releases and guidance provided to analysts and rating agencies;
- discussing policies with respect to risk assessment and risk management;
- meeting separately and periodically with management, the internal auditors and independent auditors;
- reviewing with the independent auditor any audit issues and management's responses to such issues;
- setting clear hiring policies for employees or former employees of the independent auditor; and
- reporting regularly to the board of directors.

The NYSE also requires listed companies to maintain an internal audit function, which may be satisfied by an internal department or an outside third party who is not the independent auditor, and the internal audit function must be overseen by the audit committee. The NYSE and Nasdaq rules also govern what types of matters must be addressed in audit committee charters.

Compensation Committee

NYSE- and Nasdaq-listed companies must have a compensation committee composed entirely of independent directors (subject to a limited exception for Nasdaq companies). The Nasdaq requires such a committee to be comprised of at least two members while the NYSE does not impose a minimum number of members. Each member of the compensation committee must qualify as independent under the stock exchange rules. Under these rules, when assessing the independence of a compensation committee member, the boards must take into account the following factors (in addition to the factors outlined under the Director Independence heading above):

- the source of compensation of a director, including any consulting, advisory or other compensatory fee to be paid by the company to the director; and
- whether the director is affiliated with the company or any of its affiliates.

The NYSE and Nasdaq require listed companies to have compensation committee charters, which must, among other things, include:

- the duty of the committee to review and approve and/or make recommendations to the board relating to the compensation of the listed company's executive officers; and
- the ability of the committee to retain and pay compensation advisers.

Nominating and Corporate Governance Committee

The NYSE requires listed companies to have a nominating and corporate governance committee composed entirely of independent directors to, among other things, select or recommend individuals for nomination to the board. In contrast, Nasdaq permits listed companies to select or recommend director nominees by either a majority of the listed company's independent directors or a nominating and corporate governance committee composed entirely of independent directors (subject to a limited exception set forth in Nasdaq's rules). The NYSE and Nasdaq rules also have requirements relating to nominating and corporate governance committee charters.

Board Evaluations

The NYSE generally requires listed companies to conduct self-evaluations of their boards and their audit, compensation, and nominating and corporate governance committees at least annually. However, the NYSE does not provide

specific requirements on how these evaluations should be conducted. Nasdaq does not require its listed companies to conduct a board evaluation.

Ethics and Code of Conduct

Stock exchange rules and the federal securities laws require listed companies to adopt a code of conduct applicable to their directors, officers and employees, addressing matters relating to conflicts of interest, fair dealing, compliance with law and enforcement of the code of conduct. Any waivers of the code of conduct for directors or executive officers are required to be publicly disclosed.

Corporate Governance Guidelines

Any company listed on the NYSE must adopt and disclose corporate governance guidelines that address certain matters, including:

- director qualification standards and responsibilities;
- director access to management and independent advisers;
- director compensation;
- director orientation and continuing education;
- management succession; and
- the annual performance evaluation of the board and its committees.

2. Corporate Governance Context

2.1 Hot Topics in Corporate Governance

In Delaware, directors and officers of a corporation owe fiduciary duties of care and loyalty to the corporation and its stockholders. Certain other states have adopted constituency statutes pursuant to which directors and officers of corporations are, in certain circumstances, permitted to consider the interests of constituents

other than stockholders, such as customers, employers, the community, suppliers or creditors.

Similar fiduciary duties are typically owed by the partners in a general partnership, the general partners in a limited partnership and the managers or managing members, as applicable, in an LLC. However, unlike with corporations, Delaware and certain other states permit these fiduciary duties to be limited or eliminated entirely in the entity's organisational documents.

Duty of Care

The duty of care requires a director to act in an informed and considered manner and take the care that a prudent businessperson would take when considering a business decision. To satisfy this duty, a director should review all material information reasonably available and have sufficient time to consider such information in advance of making a decision on behalf of the corporation. A director should also be afforded the opportunity to ask questions of management and outside advisers and should take advantage of this opportunity in the event the director does not understand something or believes there is an omission.

A director is also entitled to rely upon information provided by management and outside advisers in satisfying this duty, unless the director has knowledge that the reliance is unwarranted.

Duty of Loyalty

The duty of loyalty requires a director to act in the best interests of the corporation and its stockholders rather than in the director's own self-interest or the interests of some other constituency, such as a particular stockholder. To satisfy this duty, a director should either avoid situations involving a conflict of interest or dis-

close the substance of the conflict to the full board. In Delaware, the duty of loyalty also generally requires directors to make good faith efforts to oversee the corporation's operations through the implementation and monitoring of a board-level information and reporting system designed to keep the board informed of critical risks (known as the “Caremark” duty). Delaware cases have also confirmed that the Caremark duty of oversight also applies to officers with respect to matters within their areas of oversight.

Judicial Standards of Review

If directors have discharged their duties of care and loyalty, their decisions will generally be protected by the presumption of the business judgement rule, pursuant to which courts will not rescind an action of the board so long as it can be attributed to any rational business purpose. However, if a plaintiff satisfies the burden of showing that directors failed to discharge the duty of care or the duty of loyalty (such as by showing the existence of a conflict of interest or gross negligence or bad faith on the part of directors when making such decision), the board could lose the protections of the business judgement rule and its actions could be subject to a higher standard of judicial scrutiny. For example, recent decisions by Delaware courts have demonstrated an increased willingness to permit Caremark duty of loyalty claims to survive the motion to dismiss stage when the directors' failure to oversee critical risks rises to the level of bad faith.

In certain states, including Delaware, courts will apply enhanced scrutiny to board actions under certain circumstances due to the sensitive nature of the matter at issue, such as in connection with decisions to enter into a transaction constituting a change of control of the corporation or the adoption of a defensive action by the board.

See **4.8 Consequences and Enforcement of Breach of Directors' Duties** and **4.9 Other Bases for Claims/Enforcement Against Directors/Officers** for more information about the standards of review and legal implications in connection with fiduciary duty breaches.

2.2 ESG Considerations

In the USA, there is a significant amount of rule-making currently underway in respect of ESG-related disclosures. Over the last few years, the Securities and Exchange Commission (SEC) has been in the process of developing prescriptive disclosure requirements related to certain ESG topics, such as climate change, human capital management and board and workforce diversity. Most recently, this culminated in the SEC's adoption of new rules that would require public companies to provide certain climate-related information in their public reports, but the effectiveness of such rules has since been stayed due to pending legal challenges. In the absence of such prescriptive requirements, ESG matters are subject to the same principles-based approach and materiality standard that applies to other types of disclosure under the federal securities laws.

However, despite the fact that the pace of rule-making in this area has remained relatively slow, public companies have long faced pressure to voluntarily provide ESG-related disclosures. For years, institutional investors, proxy advisory firms, stockholders and other stakeholders have called on companies to provide ESG disclosures and/or enhance their ESG practices through public statements, voting guidelines and stockholder proposals. Stockholder proposals, in particular, generally serve as a low-cost way for stockholders to influence corporate behaviour and, since 2020, the number of stockholder proposals related to environmental and social mat-

ters has significantly increased year over year. There has also been a substantial increase in so-called “*anti-ESG*” proposals in recent years, reflecting the fact that ESG issues, particularly issues relating to climate change and diversity, have become increasingly polarised in the USA.

This growing divide has led some major institutional investors, including BlackRock, State Street and Vanguard, to revise their proxy voting guidelines to de-emphasise ESG as a stand-alone focus area and instead emphasise the importance of managing risks, including environmental and social risks. Failure to provide appropriate disclosures related to such issues can result in votes against the company, both on stockholder proposals and in director elections. For a discussion of examples of topical ESG issues, see the USA Trends & Developments chapter in this guide.

Companies often engage with investors on ESG matters through a broad array of channels, including providing ESG information in periodic sustainability reports, proxy statements and other public filings and hosting ESG-related conference calls. As Regulation FD prohibits selective disclosure of material, non-public information, companies that engage with investors on ESG matters in private meetings may be required to make additional public disclosure in order to satisfy their obligations under Regulation FD.

3. Management of the Company

3.1 Bodies or Functions Involved in Governance and Management Corporations

In the USA, most public companies are corporations. State law generally delegates the authority to manage the business and affairs of a corpora-

tion to the board of directors. A board of directors typically delegates day-to-day management of the corporation to its executive officers but exercises oversight over management. The boundaries of a board’s delegation to management may be documented by a board-approved delegation of authority that sets forth what types of decisions and transactions require board approval (such as transactions above a specified threshold).

The board may also delegate certain of its oversight responsibilities to its committees, including its standing committees and/or new committees established by the board for the purpose of pursuing certain objectives, such as a transaction committee to manage the execution of certain strategic transactions or a special litigation committee to address stockholder derivative litigation. However, because the board as a whole remains responsible for ensuring it is satisfying its fiduciary duties, including its oversight responsibilities, it is important for the board to receive periodic updates regarding material issues it has delegated to management or its committees.

Stockholders do not actively manage the business and affairs of a corporation, but instead exert influence on a corporation by voting, submitting stockholder proposals, privately or publicly engaging with the board and/or management or obtaining representation on the corporation’s board either by nominating director candidates for election by stockholders or reaching an agreement with the board.

Limited Liability Companies

The governance structure of an LLC depends on whether the LLC has one or more members and whether it is managed by its members or managers. A single-member LLC will typically be

managed by its sole member. A multi-member LLC may be managed by its members or by outside managers. Freedom of contract is a fundamental principle of US LLCs, so management authority in a multi-member LLC can generally be tailored in the operating agreement to the contracting parties' needs.

Partnerships

In a general partnership, each partner has the authority to undertake transactions, execute contracts and incur liabilities on behalf of the partnership, and is responsible for the day-to-day affairs of the partnership. In a limited partnership, management authority is delegated to a general partner, and limited partners generally do not have management authority over the business. A limited partner who does participate in the day-to-day management of the partnership may lose the protection of limited liability.

Similarly to LLCs, limited partnerships follow the freedom of contract principle, so management authority in a limited partnership may also be tailored to the contracting parties' preferences in the limited partnership agreement.

3.2 Decisions Made by Particular Bodies

A board of directors of a corporation in the USA typically makes decisions relating to the following matters:

- mergers and acquisitions;
- charter amendments;
- issuances of securities or equity awards;
- declarations and payments of dividends;
- selection, replacement and compensation of key executives;
- dissolution of the corporation; and
- other material corporate actions in which there is a determination that board action would be desirable.

Certain actions that are approved by the board must also be approved by stockholders under state law or the stock exchange rules, including the following actions:

- charter amendments;
- a merger involving the corporation as a target or a sale of all or substantially all of the corporation's assets;
- issuance of more than 20% of the corporation's outstanding shares of common stock;
- conversion of the corporation to another entity form;
- domestication of the corporation to a foreign jurisdiction; and
- dissolution of the corporation.

In an LLC or a partnership, decision-making authority may be tailored to the contracting parties' preferences within certain parameters set forth in the LLC operating agreement or the partnership agreement.

3.3 Decision-Making Processes

A board of directors of a corporation in the USA (including its committees) makes decisions by passing resolutions at a board or committee meeting or by acting through written consent in lieu of holding a meeting. In advance of a board or committee meeting, management or the board's outside advisers typically provide directors with a meeting agenda and written materials to ensure the directors are properly informed on the topics to be discussed at the meeting. Board meetings often include management presentations on the relevant topics and an executive session in which the board deliberates without the presence of management or any directors that are employed by the corporation.

At the meeting, the secretary of the corporation will typically keep board minutes as the official record of board deliberation and action.

Recent Delaware cases have emphasised the importance of boards adhering to corporate formalities (such as documenting board actions through minutes, resolutions and official letters). For example, stockholders are increasingly making demands in reliance on Section 220 of the DGCL, which gives stockholders the right to inspect a corporation's books and records for certain purposes, in order to gather information to criticise a corporation's decisions and decision-making processes in advance of filing lawsuits or launching activist campaigns. Under these cases, corporations that observe formalities can generally satisfy a Section 220 demand by producing those formal records only. However, corporations that instead correspond through informal channels (such as emails and text messages) may need to produce those electronic communications.

Corporations in the USA are required to hold an annual stockholders' meeting for purposes of electing directors and taking other actions, and may also call special meetings to allow stockholders to take action in between annual meetings. If permitted by applicable state law and the corporation's organisational documents, stockholders may take action by written consent in lieu of a meeting. See **5.3 Shareholder Meetings** for more information about stockholders' rights to call special meetings or act by written consent.

In an LLC or a partnership, action may be taken at meetings or by written consent, as may be set forth in the LLC operating agreement or the partnership agreement. There is generally no requirement to hold meetings.

4. Directors and Officers

4.1 Board Structure

A typical board structure for a US corporation includes a single class of directors elected annually with standing committees that are delegated authority by the board to be responsible for certain matters such as audit, compensation and corporate governance matters. The board's authority to delegate matters to committees is typically broad, and committees will generally have the full authority to exercise the power of the board, subject to limited exceptions.

Most directors in the USA are elected annually. However, many states, including Delaware, permit boards to stagger their directors into separate classes that are up for election less frequently than annually. In such cases, each director class is generally limited to a term of no longer than three years. As a result, stockholders of corporations with staggered boards only elect a portion of the board each year (eg, a third of the board). Staggered boards have become less common among US public corporations, largely due to opposition from proxy advisory firms and institutional investors who argue that such structures diminish director accountability to stockholders and promote entrenchment. See **4.4 Appointment and Removal of Directors/Officers** for more information regarding the election of directors.

4.2 Roles of Board Members

A board of directors of a public corporation is typically comprised of management directors (ie, directors who also serve as employees or officers of the corporation) and independent directors. However, there may be other directors who are not independent but also not management directors (eg, directors who are employed by a controlling stockholder of the corporation). See

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares for a discussion of how the independence of directors is determined.

Management directors generally have more intimate knowledge of the corporation's affairs as compared to independent directors. Certain states other than Delaware hold management directors to a higher standard of care due to their knowledge of and active involvement with the business. Independent directors are generally permitted to rely, within reasonable limits, on information provided by management and outside advisers in satisfying their fiduciary duties.

The board will also often appoint a chair from amongst its members to serve as the leader of the board. The chair can either be an independent director or a non-independent director. When the chair of the board is non-independent (such as the CEO of the corporation), public corporations generally appoint a lead independent director that has similar responsibilities as the chair to help ensure independent oversight of management. The specific responsibilities of the board's chair are typically laid out in the corporation's corporate governance guidelines or other organisational documents, but usually include duties such as presiding at board and stockholder meetings, establishing meeting schedules and agendas, serving as liaison between the board and management and being available, as needed, to meet with stockholders. In addition to the board chair, the board also appoints chairs of each board committee.

4.3 Board Composition Requirements/Recommendations

Composition requirements for US boards are driven by stock exchange rules, federal secu-

rities laws, state law, and proxy advisory firm guidelines.

Stock Exchange Rules

Subject to certain exceptions, both the NYSE and Nasdaq rules require a majority of a public company's board to be independent, and only independent directors may serve on the audit, compensation and/or nominating and corporate governance committees. The NYSE and Nasdaq have bright-line tests relating to whether a director qualifies as independent, which must be affirmatively determined by the board. See **1.3 Corporate Governance Requirements for Companies with Publicly Traded Shares** for a detailed discussion of the NYSE and Nasdaq requirements on director independence.

Federal Securities Laws

The federal securities laws require each member of an audit committee to be independent and provide an overlay of independence requirements for audit committee members. See **1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares** for a discussion of independence requirements under Rule 10A-3.

State Law

State law typically does not impose minimum independence requirements for company boards. However, for corporations, having independent directors may be favourable to the corporation and its directors from a stockholder litigation perspective. For example, in the context of a conflicted corporate transaction (ie, a transaction in which an officer or director has an interest on both sides of the transaction), review and approval (or ratification) of the transaction by disinterested directors (along with the implementation of other procedure protections,

such as stockholder approval) may subject such a transaction to a more deferential standard of review by the courts.

Proxy Advisory Firms Guidelines

The proxy advisory firms have published extensive guidelines that relate to board composition. ISS and Glass Lewis guidelines stress that boards should be at least a majority independent, and have fully independent audit, compensation and nominating and corporate governance committees and independent board leadership (ie, either an independent board chair or a lead independent director). ISS and Glass Lewis have also adopted board diversity policies in their proxy voting guidelines that generally provide for negative vote recommendations against the chair of the nominating and corporate governance committee of companies that fail to maintain a specified level of board diversity (either in terms of gender or racial/ethnic diversity). The specific minimum diversity thresholds differ between ISS and Glass Lewis, with Glass Lewis generally imposing a higher threshold.

Investor Expectations

Investors are increasingly focused on ensuring that boards of public corporations have a sufficient mix of skills and expertise to enable them to exercise effective oversight and make informed decisions regarding the management of the corporation. Although there are limited requirements on the specific skills and qualifications directors must have, stockholders have submitted a number of proposals over the last few years seeking the representation of specific skills on boards, such as cybersecurity, sustainability or corporate governance experts.

In response, corporations are increasingly highlighting the skills and experiences represented on their boards by publishing skill matrices or

other graphics that identify certain key skills that are relevant to the board's ability to oversee the corporation's business, such as finance and accounting, international, risk management and cybersecurity/technology expertise, and the specific directors (or aggregate number of directors) on the board that possess those skills.

4.4 Appointment and Removal of Directors/Officers

Directors of US public corporations are typically elected at stockholder meetings by the vote of a majority of the stockholders present and entitled to vote (although some corporations may have plurality voting depending on state law and the corporation's organisational documents). In majority voting, a nominee generally must receive more "for" votes than "against" or "abstain" votes to be elected (or re-elected) to the board. In plurality voting, the nominees who receive the most "for" votes are elected (or re-elected) to the board until all board seats are filled. As a result, under plurality voting, in an election where the number of nominees is equal to the number of available board seats (ie, an uncontested election), every nominee would be elected upon receiving just one "for" vote.

In most states, including Delaware, once a director has been elected, he or she may only be removed before the expiration of his or her term by the corporation's stockholders or upon his or her resignation. Typically, stockholders may remove a director with or without cause by a majority vote. However, if the board is staggered or the corporation permits cumulative voting, a director may only be removed for cause unless otherwise provided in the corporation's certificate of incorporation.

In the event there is a vacancy on the board (either because of a director's removal, resigna-

tion or death or an increase in the board's size), the stockholders or a majority of the directors still in office can generally appoint a new director to fill that vacancy unless the corporation's organisational documents provide otherwise. Officers are appointed by the board of the corporation, and the offices of a corporation are typically set forth in the corporation's by-laws or in board resolutions. An officer may be removed by the board with or without cause, subject to contractual protections in that officer's employment agreement.

4.5 Rules/Requirements Concerning Independence of Directors

See 1.3 Corporate Governance Requirements for Companies with Publicly Traded Shares and 4.3 Board Composition Requirements/Recommendations for a discussion of rules and requirements relating to director independence.

The federal securities laws and state law provide rules relating to director conflicts of interest. Under the federal securities laws, public companies are required to disclose any transaction over USD120,000 that has occurred since the last fiscal year or is currently proposed, in which the company is a participant and any "*related person*" (defined to include the company's directors, among others) has or will have a direct or indirect material interest. Whether a director's interest in a transaction is "*material*" is a fact-specific determination; however, the federal securities laws do provide a number of "*per se immateriality standards*", including if the director's interest in the transaction arises solely because he or she also serves as a director at the other company involved in transaction and/or owns less than 10% of the other company's stock. The federal securities laws also require public companies to disclose their internal policies for reviewing transactions with related per-

sons and the persons responsible for applying such policies.

Under state law, transactions in which a director has a conflict of interest may be voidable and/or subject to a duty of loyalty breach claim by a stockholder. However, most states have adopted safe harbour statutes for conflicted transactions, which provide that such transactions are not per se voidable if any of the following conditions are met:

- the material facts relating to the conflict are disclosed to the board and the transaction is approved by non-conflicted directors;
- the material facts relating to the conflict are disclosed to stockholders and the transaction is approved by non-conflicted stockholders; and/or
- the transaction is fair to the corporation.

In Delaware, the DGCL was also recently amended to provide that transactions involving conflicted directors or officers or involving controlling stockholders (other than going-private transactions) can also now be protected from both equitable relief and damages liability (including in connection with duty of loyalty claims) if they are either (i) approved by an independent board committee consisting of at least two non-conflicted directors, or (ii) approved or ratified by a majority of the votes cast by the corporation's non-conflicted stockholders.

4.6 Legal Duties of Directors/Officers

See 2.1 Hot Topics in Corporate Governance.

4.7 Responsibility/Accountability of Directors

In Delaware and many other states, directors and officers of a corporation owe fiduciary duties to the corporation as an entity and to its stock-

holders. See **2.1 Hot Topics in Corporate Governance** for more information regarding general fiduciary duties. In the case of insolvent corporations, these duties require directors and officers to manage the corporation for the benefit of all residual beneficiaries, and creditors of insolvent companies may enforce these fiduciary duties against directors.

Certain other states have various forms of constituency statutes, which permit the board in certain circumstances to balance the interests of stockholders against interests of other constituents, including customers, employers, suppliers or creditors. In addition, directors of public benefit corporations are required to consider the interests of the public, not just those of the stockholders.

In certain states, including Delaware, all partners in a general partnership, the general partners in a limited partnership and the managers or managing members in an LLC owe similar fiduciary duties to the company and to the company's other partners/members, but, unlike with corporations, these duties may be limited or eliminated entirely in the company's organisational documents.

4.8 Consequences and Enforcement of Breach of Directors' Duties

Claims against a director of a US corporation for a fiduciary duty breach may be brought directly by the corporation or by its stockholders on behalf of the corporation or, in some instances, on their own behalf. The consequences of a breach of fiduciary duty may be monetary damages or equitable relief.

A director is typically protected from personal monetary liability arising out of a breach of his or her fiduciary duty of care in several ways.

Firstly, courts typically apply the business judgement rule when reviewing the business decisions of a director in connection with an alleged duty of care breach. Because this standard of review is highly deferential to the board, it is rare for a court to find a fiduciary duty breach in decisions subject to the business judgement rule. (Note that duty of loyalty claims are generally subject to a heightened standard of review in the absence of the satisfaction of certain requirements, which means such claims are more likely to result in liability for directors.)

Secondly, states typically permit corporations to adopt provisions in their organisational documents that provide for the exculpation and/or indemnification of directors for losses and expenses incurred in connection with a duty of care claim. Indemnification rights generally apply to officers as well, and recently adopted amendments to the DGCL now permit Delaware corporations to exculpate certain senior officers in connection with direct duty of care claims brought by stockholders (but not for claims brought by the corporation or brought derivatively by stockholders on the corporation's behalf). However, state corporation law statutes generally preclude corporations from exculpating and/or indemnifying directors and officers from duty of loyalty claims.

Thirdly, states typically permit corporations to purchase liability insurance for their directors to cover losses resulting from fiduciary duty claims, including duty of care and loyalty claims.

4.9 Other Bases for Claims/Enforcement Against Directors/Officers

Courts evaluate board action under different standards of review, depending on the facts and circumstances underlying the board action. As discussed in **2. Corporate Governance Context**,

business judgement review is the default standard for courts to review board action. If a plaintiff satisfies the burden of rebutting a presumption underpinning the business judgement rule, courts in most states apply “*entire fairness*”, the most onerous standard of review, to board action, which requires the board to establish that a transaction was a product of fair dealing and fair price.

Courts in certain states, such as Delaware, apply enhanced scrutiny (which is an intermediate standard of review) to board action in certain circumstances, regardless of whether the presumptions underlying the business judgement rule have been satisfied, such as a board’s decision to enter into a transaction constituting a change of control of the corporation or to adopt a defensive action in response to a threat, such as adopting a poison pill. In circumstances where enhanced scrutiny applies, boards are required to take certain actions that they would not otherwise be required to take, such as seeking a transaction offering the best value reasonably available to stockholders in a change-of-control scenario.

Breaches of Corporate Governance Requirements

In addition to the core fiduciary duties of care and loyalty, Delaware and many other states recognise certain other corporate law doctrines that can support claims against directors or officers for breaches of corporate governance requirements. For example, in Delaware, board action that is intended primarily to interfere with the stockholder “*franchise*” ie, core rights incident to share ownership, such as voting rights – must be justified by demonstrating a compelling justification for taking such action. Another example is the corporate waste doctrine, under which directors have a duty not to approve “*wasteful*”

transaction, which no person of ordinarily sound business judgement would find fair or acceptable.

Delaware law also imposes on directors a duty to disclose all material information in certain circumstances, including self-dealing transactions.

For a discussion of limitations on director and officer liabilities, see **4.6 Legal Duties of Directors/Officers**.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

Compensation for executive officers and directors of US corporations generally must be determined by the board of directors, and this responsibility is often delegated to compensation committees (or nominating and corporate governance committees, in the case of director compensation). In Delaware, the board’s decisions regarding executive compensation are generally protected by the more deferential business judgement rule. However, a conflict of interest resulting in application of the entire fairness standard may arise where directors approve compensation arrangements for themselves or for officers that are also controlling stockholders of the corporation.

The federal securities laws require public companies to convene a stockholder vote to approve, on an advisory basis, the compensation of the company’s named executive officers (generally, for corporations, the CEO, CFO and three other most highly compensated executive officers), commonly referred to as the “*say-on-pay*” vote, at least once every three years and a separate vote to determine how often the say-on-pay vote will be held (“*say-when-on-pay*”) at least once every six years.

The NYSE and Nasdaq listing standards also require listed companies to receive stockholder approval for most equity compensation plans (and material amendments thereto).

4.11 Disclosure of Payments to Directors/Officers

The federal securities laws require extensive disclosure regarding the compensation of executive officers and directors in a public company's proxy statement. The disclosure focuses on compensation for the company's named executive officers (as described in **4.10 Approvals and Restrictions Concerning Payments to Directors/Officers**); however, additional executives may be included in this group because of turnovers during the applicable year.

The company's Compensation Discussion and Analysis (CD&A) in its annual proxy statement must explain the material elements of the company's compensation for its named executive officers and is intended to facilitate investors' understanding of the numbers in the requisite tables that follow the CD&A. A short compensation committee report is also required to be included in the proxy statement. Disclosure of any policies or practices regarding the ability of employees and directors to engage in hedging transactions with respect to the company's securities is also required.

Summary Compensation Table

The main table required to be included in a company's proxy statement is the Summary Compensation Table, which generally discloses the compensation earned by each named executive officer for each of the prior three fiscal years by category: salary, bonus, stock awards, options awards, non-equity incentive plan compensation, change in pension value and non-qualified

deferred compensation earnings, other compensation and total compensation.

The SEC's "*pay-for-performance*" rules also require companies to include a table containing specific executive compensation and financial performance measures for the five most recent fiscal years, as well as narrative disclosure explaining the relationship between the compensation paid to each named executive officer and the performance of the company. Other required tables must include information relating to grants of equity and bonus awards made to each named executive officer in the last fiscal year, outstanding equity awards at the end of the last fiscal year, stock options exercised by the named executive officers and stock awards that have vested during the last fiscal year, pension benefits, and non-qualified deferred compensation.

Narrative or tabular disclosure regarding the circumstances in which a named executive officer may be entitled to compensation upon termination of employment or in connection with a change in control, including estimates of potential payouts, is also required.

Companies must also disclose the ratio between the CEO's annual total compensation and the median of the annual total compensation of all other employees.

Director Compensation

Director compensation for the most recent fiscal year is also required to be disclosed in a table that is similar to the Summary Compensation Table, along with related narrative disclosure.

5. Shareholders

5.1 Relationship Between Companies and Shareholders

Stockholders are the owners of a corporation. This ownership relationship is governed by state law. If the corporation is public and listed on a stock exchange, this relationship will also be governed by stock exchange rules and the federal securities laws. Some corporations (but few public companies) may also have stockholder agreements in place that impose additional rights or restrictions on stockholders.

5.2 Role of Shareholders in Company Management

Under state law, stockholders have no involvement in the management of a corporation, which is vested in a board of directors and often delegated to executive officers by the board. State law generally enumerates certain actions that require stockholder approval, which is further discussed in **3.1 Bodies or Functions Involved in Governance and Management**.

5.3 Shareholder Meetings

Annual meetings of stockholders of a corporation are generally required under state law for the election of directors. For example, in Delaware, if a corporation fails to hold its annual meeting 30 days after the date designated for the annual meeting or 13 months after its last annual meeting, the Delaware Court of Chancery may order a stockholder meeting upon the application of any stockholder or director.

Special meetings of stockholders may be called by the board of directors or any other person authorised by a corporation's organisational documents, such as stockholders. Corporations may explicitly prohibit the ability of stockholders to call special meetings in their organisational

documents as a defence against stockholder activism. Most corporations that permit stockholders to call special meetings impose certain procedural requirements in their organisational documents that restrict such a right (such as ownership thresholds, informational requirements and blackout periods). Such restrictions must be contained in the corporation's certificate of incorporation or by-laws.

State law governs the mechanics of holding a stockholder meeting. In Delaware, the location and time of annual meetings may be established in a corporation's organisational documents or by the board. Such meetings can also be held virtually (by means of remote communication) if permitted by the corporation's organisational documents. Written notice of a meeting must be given to stockholders entitled to vote no later than ten days and no earlier than 60 days before the date of the meeting. The board is required to fix a record date for the purpose of establishing which stockholders are entitled to notice and the right to vote at a stockholder meeting, which must be no later than ten days and no earlier than 60 days before the date of the meeting.

Quorum requirements may be set in a corporation's organisational documents but may not be less than one third of the shares entitled to vote at the meeting. Delaware law generally does not govern the type of business to be conducted at a stockholder meeting, but corporations may include rules in their organisational documents or publish rules and/or agendas that impose restrictions on the proposals that can be acted on at a meeting. For example, it is common for public corporations to adopt advance notice by-laws, which require stockholders wishing to nominate a director or make a stockholder proposal to satisfy rigorous procedural and substantive requirements in order for their nomina-

tion or proposal to be properly raised at a stockholder meeting.

In Delaware, stockholders, by default, have the right to take action by written consent without holding a stockholder meeting unless prohibited by the corporation's certificate of incorporation. Most public corporations prohibit stockholder action by written consent in their certificates of incorporation.

5.4 Shareholder Claims

A stockholder of a US corporation may file (i) direct claims against the corporation or its officers and directors for actions that directly harm the stockholder or (ii) derivative claims against the corporation's officers and directors for actions that harm the corporation. A common example of a derivative claim brought by a stockholder is a claim alleging a breach of fiduciary duty by the board.

Prior to filing a derivative claim, a stockholder must demand that the board pursue the claim or, in most states, including Delaware, demonstrate that such a demand is futile because of the board's conflict of interest with respect to the litigation. This procedural requirement does not exist for direct claims, so stockholders at times try to refashion derivative claims as direct claims.

5.5 Disclosure by Shareholders in Publicly Traded Companies

Federal Securities Law

The federal securities law requires an investor or group of investors who acquire beneficial ownership of more than 5% of a public company's voting equity securities to file reports relating to their ownership on Schedule 13D, or if eligible, on Schedule 13G. Passive investors that own less than 20% of a company's equity securities

are eligible to report that ownership on Schedule 13G, and are otherwise subject to a less onerous reporting regime than that applicable to Schedule 13G filers. An investor who acquires more than 5% of a public company's voting equity securities, and is not eligible to file a Schedule 13G, must report the acquisition on a Schedule 13D with the SEC within five business days of crossing the 5% threshold.

Schedule 13D requires the disclosure of the identity of the investor, information about the investor's ownership of the company's securities and sources of funds, any of the investor's arrangements with respect to securities of the company and the purpose of the acquisition, including any plans or proposals which the investor may have to make changes to the board or management or to consummate a corporate transaction. The Schedule 13D must be amended to reflect any material changes in the disclosure contained in the original Schedule 13D (including the acquisition or disposition of 1% or more of the class of equity securities of the corporation) within two business days of such change. Subject to certain exceptions, an investor eligible to file a Schedule 13G must file the report within 45 days after the end of the calendar quarter in which the investor first became obliged to make such a filing.

Institutional Investment Managers

Institutional investment managers that have assets under management of at least USD100 million must report to the SEC their holdings of exchange-traded equity securities, certain equity options and warrants, shares of closed-end investment companies and certain convertible debt securities on Form 13F within 45 days of the end of each calendar quarter. Form 13F requires disclosure of the name of the manager, the name and class of security holdings and the

number of shares and the market value of such shares as of the end of the calendar quarter.

Beneficial Owners

Beneficial owners of more than 10% of any class of equity security of a public company (as well as directors and officers) must report their beneficial ownership of equity securities on Section 16 forms. Transactions in equity securities by such stockholders, directors and officers must generally be reported within two business days. These parties may be required to disgorge to the company any profits made in connection with the purchase and sale of the company's securities within a six-month period.

Acquisitions of Voting Securities

Certain acquisitions of voting securities by an investor must be reported to the Federal Trade Commission (FTC) and the Department of Justice (DOJ) prior to consummation if the transaction value and the sizes of the investor and issuer exceed certain thresholds pursuant to the Hart-Scott-Rodino Antitrust Improvements Act. Upon the investor making the filing, the FTC and DOJ have a 30-day period in which to request further information from the investor to determine whether the acquisition violates the US antitrust laws.

The contents of the filing are confidential. Stockholders should be mindful of other regulatory regimes that may be implicated by a stockholder's acquisition of shares, including:

- the Committee on Foreign Investment in the United States for certain acquisitions by foreign persons;
- the Federal Energy Regulatory Commission for acquisitions of the shares of regulated utilities; and

- the Federal Communications Commission for acquisitions of the shares of regulated telecommunication companies.

6. Corporate Reporting and Other Disclosures

6.1 Financial Reporting

The federal securities laws require public companies to file publicly annual, quarterly and current reports relating to the occurrence of certain events material to stockholders. Annual and quarterly reports must be certified as accurate and complete by a company's CEO and CFO. Public companies are also required to file proxy statements in connection with their stockholder meetings.

6.2 Disclosure of Corporate Governance Arrangements

The federal securities laws require public companies to disclose the following information relating to corporate governance in their proxy statements:

- director biographical and qualification information;
- director independence and the methodology for determining director independence;
- board meeting attendance and related policies;
- committee information, including membership, purpose and function, and number of meetings held;
- the board's leadership structure;
- the board's role in risk oversight;
- applicable hedging policies regarding director ownership of stock;
- the company's code of ethics or rationale for non-adoption;

- compensation of the named executive officers, including the CD&A;
- certain pay ratios and say-on-pay policies; and
- independent auditor information.

Public companies must also disclose the occurrence of certain events in a current report, including:

- a change in control;
- the election or departure of a director or officer;
- any amendment to certain organisational documents;
- any amendment to the company's code of ethics, or waiver of a provision of the code of ethics;
- the voting results of any matters submitted to a vote of stockholders;
- stockholder director nominations; or
- changes in a company's certifying accountant.

The federal securities laws also require a public company to post on its website the charters of its audit, compensation and nominating and corporate governance committees or include the charters as an appendix to its proxy statement every three years. NYSE requires listed companies to make their codes of ethics publicly available on or through its website.

6.3 Companies Registry Filings

State law generally requires corporations and certain other entity forms to file the certificate of incorporation for the corporation with the Secretary of State. Certain states also require corporations and certain other entity forms to file annual or biannual reports, which generally require basic information about the entity, such as its legal name, address, registered agent and

names of directors and officers. States typically make these filings publicly available.

7. Audit, Risk and Internal Controls

7.1 Appointment of External Auditors

The federal securities laws require public companies to have an independent auditor review their financial statements and disclosures and provide an opinion as to their fairness and compliance with the Generally Accepted Accounting Principles (GAAP).

The SEC considers the independence of an auditor impaired if the auditor is not, or if a reasonable investor with knowledge of all attendant facts and circumstances would conclude that the auditor is not, capable of exercising impartial judgement on all issues encompassed within the audit engagement. In addition, certain actions and arrangements between a company and its outside auditor are not permitted, including contingent fee arrangements, direct or material indirect business arrangements between a company and its outside auditor and a company hiring certain employees of the independent auditor during a one-year cooling-off period.

SEC rules prohibit independent auditors from providing certain non-audit services to a company, including but not limited to bookkeeping, management or human resource functions or legal services and unrelated expert advice. Independent auditors may provide other non-audit services to a company that are not specifically prohibited by SEC rules as long as the audit committee pre-approves such services. A company's audit committee is responsible for the oversight of its independent auditor.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The federal securities laws require a public company to maintain adequate internal controls over financial reporting (ICFR) in order to provide reasonable assurances with respect to the reliability of the company's financial reporting and compliance with GAAP measures. A company's principal executive and financial officers are responsible for the design and implementation of the internal ICFR regime and must report control deficiencies and related findings to the audit committee and the company's independent auditor. Subject to certain exceptions, companies are required to include a management-drafted internal control report with their annual report and a related attestation by the company's independent auditor.

The NYSE requires a company's audit committee to discuss policies with respect to risk assessment and risk management, but states that the audit committee is not required to be the sole body responsible for risk oversight. The federal securities laws require disclosure of the board's role in the company's risk oversight process, including with respect to cybersecurity risks. However, in response to investor, proxy adviser and stakeholder pressure, many companies go beyond these requirements to provide more detailed risk oversight disclosures, particularly in proxy statements, often including descriptions of their risk oversight processes for other critical risks facing the company and/or describing the number of directors the company has that have risk oversight experience.

Trends and Developments

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Sullivan & Cromwell LLP has a record of success and client service, which has been perfected over 140 years and made the firm one of the models for the modern practice of law. Today, it is considered one of the leaders in each of its core practice areas and geographic markets. S&C advises a diverse range of clients on

corporate governance, corporate transactions, litigation and estate planning matters. It comprises more than 875 lawyers, who conduct a seamless, global practice through a network of 13 offices located in Asia, Australia, Europe and the USA.

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Introduction

Corporate governance reforms continue to be an important topic for US companies. This article will cover the key topical issues at the time of publication in 2025.

Companies Face Continued Political and Economic Uncertainty

Companies are facing an increasingly challenging business environment driven by ongoing political and regulatory developments, policy shifts and economic volatility. For example, President Trump has already issued multiple executive orders that alter the regulatory landscape, including orders directing all executive departments and agencies to (i) freeze all rule-making activity (including the issuance, proposal and publication of any new rules or other regulatory actions) until they can be reviewed and approved by a presidential appointee; and (ii) initiate processes to identify and rescind/modify regulations deemed to be inconsistent with the administration's policies. While it is not uncommon for incoming administrations to implement regulatory freezes or rescind prior rules, the high amount of regulatory activity during the Biden administration, including in key areas such as cybersecurity/data privacy, AI and consumer protections, means these orders could meaningfully impact a number of new and pending regulations with which companies may have already started to comply.

Major policy shifts at the U.S. Securities and Exchange Commission (the SEC) are also expected under the direction of new Chair Paul Atkins. To date, the SEC has dropped several of its high-profile cases and enforcement actions against crypto companies and ended its defence of the landmark climate disclosure rules adopted under the prior administration (which have not yet become effective due to ongoing legal

challenges). In February, the Staff of the SEC's Division of Corporation Finance also issued new guidance and interpretations that may make it more difficult for shareholders to engage with companies on ESG-related issues going forward, including (i) a new legal bulletin rescinding 2021 guidance that had narrowed the ability of companies to exclude shareholder proposals with "*broad societal impact*" from their proxy statements; and (ii) a revised Compliance and Disclosure Interpretation addressing circumstances in which a shareholder's engagement with a company's management on ESG and other matters could result in the shareholder losing its eligibility to report beneficial ownership on the short-form Schedule 13G and instead require reporting on the more disclosure-intensive Schedule 13D. These changes have already started to impact the 2025 proxy season, with shareholder proponents withdrawing environmental and social proposals at much higher rates, and the SEC granting no-action requests for such proposals far more frequently than in previous years. In terms of future SEC priorities, according to Chair Atkins' testimony during his Senate confirmation hearing, key focus areas during his tenure will include matters like developing a regulatory framework for digital assets, facilitating capital formation and scaling back "*[u]nclear, overly politicized, complicated, and burdensome regulations*" to instead focus more on disclosure of financially material information.

In addition to political and regulatory shifts, companies are also facing uncertainty as a result of rising geopolitical tensions and concerns over issues like tariffs, trade policies and taxation. Given the impact such factors can have on corporate performance, investors are increasingly looking for companies to disclose how their boards and management oversee and manage macroeconomic risks, and investors have

demonstrated an increased willingness to hold directors accountable for perceived oversight or disclosure failures.

In this rapidly changing environment, it is important for business leaders to stay apprised of new and ongoing developments and consider their impact on their company's strategic plans, operations and risk profiles. Boards may also want to consider requesting more frequent updates from management on key developments that could materially impact their business and, in some cases, even ask management to review and test assumptions and sensitivities underlying their company's strategic plans to ensure different potential scenarios are taken into account, if appropriate. Additionally, companies should also consider preparing responses to possible shareholder questions regarding how they are navigating these ongoing political, regulatory, economic and social uncertainties.

Corporate DEI Practices Face Growing Scrutiny

Although there is still a significant amount of uncertainty regarding the new administration's priorities and policies, one area that has become a clear area of scrutiny for regulators and politicians is diversity, equity and inclusion (DEI).

The legal basis for DEI attacks stems, in part, from the U.S. Supreme Court's June 2023 decision in *Students for Fair Admissions v. Harvard*, in which the Court struck down race-based affirmative action programmes in college and university admissions based on Title VI of the Civil Rights Act of 1964, which prohibits discrimination based on race, colour or national origin in connection with programmes/activities that receive federal financial assistance. While the Harvard decision does not directly apply to private corporations, in its wake, US companies

have faced increased legal challenges to their corporate DEI programmes, including, most recently, from federal regulators.

Consistent with President Trump's campaign promises, over the last few months, the administration has taken significant actions to roll back private sector DEI initiatives through executive orders. These executive orders, among other things, direct the U.S. Attorney General, in consultation with the heads of relevant federal agencies, to identify private sector companies with "*egregious and discriminatory*" DEI programmes, signalling the possibility of potential investigations, lawsuits or other regulatory actions against publicly traded companies and large nonprofits. The U.S. Department of Justice (the DOJ) and the U.S. Office of Personnel Management have since issued internal memoranda implementing these executive orders, including one memorandum describing the steps the DOJ plans to take to "*investigate, eliminate, and penalize illegal DEI and [accessibility] preferences, mandates, policies, programs, and activities in the private sector*", including the possible use of criminal investigations.

In response to these developments, many companies are re-examining their DEI policies and activities, including any DEI-related representation goals (eg, for their boards, management, employees, suppliers and/or vendors), compensation metrics and public disclosures.

Many proxy advisers and institutional investors have also revised their voting policies and guidelines to reflect the fact that they are under increased scrutiny with respect to DEI. For example, ISS has indefinitely halted its consideration of gender, racial or ethnic diversity when making voting recommendations with respect to the election of directors at US companies, while

Glass Lewis has stated it will continue to apply its diversity-related voting policies but will now flag for its clients any recommendations that it makes with respect to the election of directors that are based, at least in part, on diversity considerations.

The DEI landscape is likely to continue to evolve in the coming months. As a result, it will be important for public and private companies to continue to monitor these developments and periodically review their DEI policies and disclosures to assess potential risks.

Evolving Approaches to Artificial Intelligence

As corporate uses of AI become more common, investors are calling on companies to provide greater transparency into how companies govern, oversee and manage the risks related to AI. For example, according to data from ISS, shareholder proposals related to AI more than quadrupled between 2023 and 2024. These proposals typically request that the targeted company (i) disclose information about AI use and/or management of related risks; (ii) conduct a third-party evaluation about AI-related risks and impacts; and/or (iii) establish a formal board-level committee to oversee AI. In 2024, AI-related proposals that went to a vote received, on average, support from 20% of votes cast, and none passed. However, a few notable examples received significantly higher levels of support (including 43% at Netflix and 37.5% at Apple).

Glass Lewis also added a new section related to AI oversight in its 2025 voting guidelines. Under this policy, while Glass Lewis will generally not make voting recommendations on the basis of a company's AI oversight practices or disclosure, in cases where there is evidence that insufficient oversight and/or management of AI technologies has resulted in material harm to shareholders,

Glass Lewis may recommend against directors if it finds the board's oversight of, response to or disclosures concerning AI-related issues to be insufficient.

As a result, companies are increasingly including AI-related information in their public filings (most commonly, in their 10-Ks and/or proxy statements), including identifying any material risks AI poses to their business and how such risks are overseen at the board and/or management level. Some companies that rely on AI for material services or operations are, with board oversight, also developing internal frameworks to govern their use of AI, including policies, guidelines and controls to ensure such use complies with their company's goals and legal, regulatory and ethical obligations.

Boards themselves are also employing a variety of methods to deepen their directors' understanding of AI, including having directors participate in education sessions with management about their company's use of AI and related risks and opportunities, bringing in external specialists to discuss AI-related trends and developments periodically and/or appointing directors with specific AI experience (though the latter is less common).

While corporate practices and disclosures related to AI continue to evolve, companies should also be aware of a number of recent regulatory enforcement actions and shareholder lawsuits that have been filed against companies (and their executives) for alleged misrepresentations related to their AI capabilities, usage and/or metrics (often referred to as "*AI washing*" lawsuits). Companies should consider subjecting any AI-related public statements to similar internal review and compliance processes as their other public disclosures.

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