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SHAREHOLDERS ROLE IN CORPORATE FINANCE: A COMPARISON BETWEEN THE US AND EUROPE

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INTRODUZIONE

Questa tesi ha lo scopo di affrontare una delle tematiche più dibattute nell'ambito della governance societaria: il ruolo che ricoprono i soci nella partecipazione alla gestione delle società per azioni, in particolare di quelle quotate. Il primo capitolo si apre con la definzione di "corporate governance" e l'illustrazione dei vari modelli esistenti per poi passare, nella seconda parte, all'analisi dei problemi di agenzia e delle strategie normative finalizzate alla loro soluzione. Nel secondo capitolo si affrontano le problematiche relative al ruolo dei soci ed ai poteri ad essi conferiti in occasione di cambiamenti nell'assetto societario. Il capitolo conclusivo analizza infine la proposta del Professor Bebchuk relativa ad un maggior coinvolgimento dei soci nelle società quotate americane. Nella parte conlusiva si esaminano anche le obiezioni al modello da lui proposto per giungere alla conclusione che, tanto in Europa quanto in America, l'attribuzione ai soci di maggiori poteri risulta essere necessaria ai fini di un miglioramento della gestione societaria.

Partendo quindi dalla definizione di "corporate governance", il mio lavoro si preoccupa di affrontare le svariate problematiche che sono ricollegabili alla gestione delle società, con particolare riferimento a quelle quotate. Si è cercato di creare un chiaro panorama di come le varie giurisdizioni prese in considerazione hanno risolto o comunque affrontato le dinamiche oggetto di recente dibattito. Ciò che è apparso evidente sono le differenze che contraddistinguono i vari sistemi legali relativamente al conferimento di poteri nelle mani dei soci. Tali differenze sono emerse grazie ad una comparazione tra il sistema presente in Europa e quello negli Stati Uniti, e per quest'ultimo, particolare attenzione è stata riservata alla disciplina dettata nello stato del Delaware, sede di moltissime società quotate. L'analisi condotta non prescinde da una valutazione storica e comparativa delle varie discipline presenti in materia di corporate governance; la legislazione societaria ha infatti dissimili punti di partenza che hanno dato luogo alla nascita di sistemi diversi in cui l'allocazione dei poteri tra i amministratori e soci segue sentieri diversi a seconda della regolamentazione che si prende in considerazione.

Ad oggi stiamo assistendo ad un cambiamento della disciplina americana in tema di società, cambiamento che sembra delineare un graduale scardinamento dei principi fondamentali che l'hanno caratterizzata per decenni e che tuttavia vede ancora l'attribuzione dei maggiori poteri nelle mani dei manager. I paesi centrali dell'Unione Europea come la Germania, l'Italia, la Francia e la Spagna, hanno avuto come punti di partenza differenti premesse e differenti sistemi giuridici, in particolare nell'ambito delle società, presentando peculiarità nella gestione delle stesse. Ad oggi grazie all'introduzione della disciplina europea, (direttive, regolamenti, raccomandazioni), si è arrivati ad avere diversi sistemi societari che però condividono gli stessi principi fondamentali e vivono attraverso dinamiche simili. A livello comunitario è stata introdotta una nuova legislazione in materia di società, relativa in particolare a quelle quotate, con lo scopo di armonizzare la disciplina in materia. La finalità ultima degli interventi del Legislatore comunitario è che, con la realizzazione di un libero mercato interno, le società nei vari paesi membri dell'Unione, operino sulla base di regole cardine fisse e che da ciò derivi una facilitazione della gestione delle dinamiche societarie.
Esistono due stutture essenziali di governance, quella monistica e quella dualistica; a partire da questi modelli base si sono delineati altri sistemi che differiscono da essi caratterizzandoli con specifiche peculiarità.
I problemi di governance, soprattutto negli Stati Uniti, sono strettamente legati alla definizione del ruolo dei soci; la necessità di un loro maggiore coinvolgimento è emersa con evidenza a seguito della crisi finanziaria del 2007/2008 in cui la mancanza di sorveglianza da parte dei soci ha contribuito al collasso di grandi società.
Molte società americane hanno colmato le lacune lasciate dal Legislatore attraverso il "private ordering": un meccanismo per cui le parti private contrattano le regole di conduzione societaria piuttosto che fare riferimento unicamente alla regolamentazione vigente.

Le disposizioni in materia di corporate governance ricoprono due funzioni fondamentali: la prima consiste nella necessità di disciplinare la vita societaria, dettando le regole per la sua conduzione. La seconda funzione è controllare e minimizzare i problemi di agenzia

che posso nascere tra soci, manager e parti terze (ad esempio i creditori). Per problemi di agenzia si intendono quei problemi che nascono quando il benessere di una parte, detta *principal*, dipende dagli atti posti in essere da un'altra parte, detta agent. Il problema sta nel motivare l'*agent* ad agire nell'interesse del *principal* piuttosto che soltanto nel proprio. Il nodo principale alla base dei problemi di agenzia risiede nel fatto che l'*agent* possiede migliori informazioni del *principal* sui fatti rilevanti e quest'ultimo non può essere certo, salvo sostenere costi notevoli, che la prestazione offerta dall'*agent* corrisponda precisamente a ciò che gli era stato promesso. Ciò determina il fatto che il valore della prestazione dell'*agent* per il *principal* si ridurrà, sia in via diretta, sia perché, al fine di accertare la qualità della prestazione, il *principal* dovrà intraprendere un costoso monitoraggio dell'*agent*.
I Legislatori dei diversi Paesi affrontano i problemi di agenzia attraverso l'utilizzo di strategie normative, da intendersi come l'impiego di strumenti di diritto sostanziale per mitigare la vulnerabilità dei *principal* di fronte all'opportunismo dei loro agent. Una buona corporate governance è tale se riesce a facilitare il processo di delegazione delle decisioni, essendo il diritto societario ancora riluttante a prevedere una più incisiva partecipazione diretta dei soci. Si assiste ad un cambio di rotta nella disciplina societaria in Europa attraverso direttive che hanno il dichiarato scopo di attribuire maggiori poteri ai soci. La Direttiva (UE) 2017/828 ha recentemente emendato la fondamentale Direttiva 2007/36: entrambe finalizzate ad un maggior coinvolgimento dei soci nelle decisioni influenti sul lungo termine.

I problemi di agenzia emergono in maniera più evidente in occasione di grandi cambiamenti idonei a modificare l'assetto societario e che possono mettere in pericolo gli interessi dei soci e delle altre parti coinvolte. Il diritto societario interviene nella regolamentazione con lo scopo di mitigare l'opportunismo che può crearsi in tali situazioni. Quando si tratta di prendere decisioni determinanti per la vita della società, come ad esempio le modifiche all'atto costitutivo, la disciplina dettata in Europa e quella presente negli Stati Uniti presenta sostanziali differenze.

La disciplina americana, in particolare quella del Delaware, prevede che le proposte di modificazione dell'atto costitutivo possano pervenire solo da parte del consiglio di amministrazione, non attribuendo nessun potere propositivo ai soci, e richiedendo l'approvazione della maggioranza semplice in sede di assemblea. La legge americana stabilisce quindi un veto bilaterale per cui né il consiglio né i soci possono apportare modifiche da soli. Al contrario la legislazione europea conferisce la possibilità di apportare modifiche all'atto costitutivo senza la necessaria iniziativa da parte del consiglio di amministrazione. Con riferimento a operazioni straordinarie, ad esempio le fusioni, la terza direttiva societaria sostituita dalla Direttiva 2011/35, stabilisce una soglia minima di due terzi dei voti all'assemblea dei soci. Negli Stati Uniti invece, è necessaria l'approvazione della maggioranza semplice per poter procedere a fusioni e acquisizioni, e - a differenza di quanto avviene in Europa - l'approvazione dei soci è necessaria per una quantità più ristretta di operazioni. Un' ulteriore differenza è di facile riscontro in tema di emissioni di nuove azioni che secondo la disciplina americana possono essere emesse sul mercato a discrezione del consiglio di amministrazione. Nel vecchio continente invece per la stessa operazione è prevista la necessaria autorizzazione dei soci nonché la conseguente attribuzione del diritto di prelazione spettante ai soci già esistenti. Questi esempi riportati dimostrano chiaramente quanto le giurisdizioni europee e quelle americane siano differenti nell' attribuire un ruolo più o meno marginale alla compagine sociale.
La realtà societaria americana è formata dalla cosiddetta "dispersed ownership", ossia una moltitudine di piccoli azionisti rappresentanti piccolissime percentuali di proprietà nell' assetto societario, a differenza della realtà europea, in cui le società sono possedute da grandi soci di maggioranza quali famiglie, banche o fondi di investimento. Le differenze nella disciplina rispondono quindi ad esigenze diverse ed ai diversi interessi delle parti coinvolte.

Questa tesi è stata ispirata dalla lettura di un articolo scritto dal Professore Lucian Bebchuk e pubblicato nella Harvard Law Review nel 2005. L'articolo, titolato "The case for increasing shareholder power" ha la finalità, come l'autore ammette, di considerare una possibile riallocazione dei poteri tra il consiglio di amministrazione ed i soci nelle società quotate con una dispersa compagine sociale. L'autore suggerisce essenzialmente di attribuire maggiori poteri ai soci motivando la sua proposta grazie ai benefici conseguenti ad un abbassamento dei costi di agenzia ed una migliore gestione della società derivanti dall'aumento di coinvolgimento dei soci stessi nelle scelte societarie.

Questo articolo ha prodotto svariate reazioni da parte del mondo accademico che hanno acceso un dibattito produttivo finalizzato a considerare la bontà delle idee proposte.

L'idea di Bebchuck prevede la sostituzione del tradizionale "director-centered system" con un modello di sua "invenzione" in cui gli amministratori detengono ancora le redini della società, ma che vedono i soci dotati del potere di cambiare l'atto costitutivo, autorizzare fusioni o cambiamenti fondamentali per la vita societaria. Il modello dai lui proposto in realtà ha prodotto tanto scalpore solo in virtù del fatto che il ruolo dei soci nella vita della società è sempre stato considerato marginale nel sistema americano. Le idee presentate dal professore sono in verità idee che sono gia state trasformate in realtà pratica nel sistema europeo che ha sempre visto i soci come soggetti determinanti nella gestione delle società stesse.

Durante le ricerche condotte è risultato evidente che i dubbi riguardo i benefici, conseguenti ad maggiore coinvolgimento dei soci risultano essere infondati. I soci infatti si troverebbero a essere maggiormente partecipi soprattutto in presenza di società con performance negative ed un loro coinvolgimento non potrebbe che giovare. In ambito europeo i legislatori nazionali ricoprono un ruolo determinante nell'attribuzione di poteri maggiori ai soci in quanto alla legislazione comunitaria è delegato solamente il ruolo di armonizzazione e di definizione di principi cardine. Un maggiore coinvolgimento dei soci all'interno delle assemble è chiaramente piu dispendioso dal punto di vista logistico e temporale, ma fa parte di un processo di miglioramento inevitabile della governance societaria. Nella stessa direzione, seppur più lentamente, sembra dirigersi anche il Legislatore statunitense, mosso dal crescente scontento dei soci che aspirano a maggiori poteri.

OVERVIEW

This dissertation has the aim of dealing with one of the current most debated topic related to corporate governance, the role that shareholders should have in the corporate finance of corporations in particular focusing of the listed ones. The first chapter begins with the definition of corporate governance followed by the examination of the various existing models. The second part of the same chapter takes into consideration the agency problems and the legal strategies adopted by the various legislators finalized to the solution of them. The second chapter concerns the role of the shareholders in occasion of fundamental changes that occur to the companies. The final chapter analyses the model proposed by Professor Bebchuk of a major engagement of shareholders in the management of US corporations. The following part of the thesis takes into consideration the comments that his proposal has triggered; the conclusion reached is that a shareholder empowerment would be a necessary step for a good corporate governance both in the EU and in the US.

Starting from the definition of "corporate governance" this thesis explores a wide range of contemporary issues related to the management of public firms with the scope of creating a clear panorama of the current situation in the different jurisdictions. My work seeks to understand certain legal and attitudinal differences relating to shareholder's powers between the United States and other civil and common law jurisdictions highlighting the peculiarity of each system and comparing the various models solving the agency problems.
The various issues are examined from a comparative and historical perspectives in order to make clear how the various jurisdictions taken into consideration have dealt with them. During the investigation it has been clarified that US and EU corporate law have different

organizational origins and, as a result of these dissimilar starting points, have followed quite different paths from the early 20th century onwards in creating a model of corporate governance.

We are now witnessing a US law that is slowly shifting from a rigid corporate law system, which started from chartered corporations to a far more liberal and flexible system, but a system in which corporate managers still held the reins of corporate power and where the participatory role of shareholders in US corporate governance was and still is very limited. The central European countries such as Germany, Italy, France and Spain, have begun with different premises and different corporate systems; each one of these jurisdictions was characterized by its own peculiarities; now, thanks to the introduction of EU provisions, whether directives or regulations or even simple recommendations, have moved to a shared system based on the same common ground which however is rich of exceptions. With the formation, and even more with the strengthening of the EU, in fact, new corporate laws entered into force and this led to the creation of common and shared principles that rendered almost uniform the corporate governance in the European Union. There are two basic models of governance, the dualistic and the monistic ones; both of them presenting variations in some internal mechanisms. Obviously, as I have specified during the dissertation it is still a long way to enjoy the perfect corporate governance and to see the elimination of the single peculiarities, but so far the European corporate law can be seen as deep inserted in every jurisdiction. The United Kingdom, on the other hand, shifted from a "free contracting" position, which evolved from unincorporated deed of settlement companies, to a system where shareholders received stronger rights as a result of compulsory participatory rights and various statutory protections.

The distinctive trajectory of US corporate governance goes some way to explaining why activism first developed in the United States, why it continues to be such a controversial issue today, and why institutional investors are increasingly using private ordering remedies to acquire governance rights that are already available to shareholders in other common law jurisdictions.

The law ruling the corporate governance has two essential roles: first it establishes the organization of the company and the rules necessary to manage it and, second it has the aim of controlling and solving possible conflicts among shareholders or "outsiders" such as minority shareholders and creditors. These kind of problems are commonly known as "agency problems" which can be defined as the conflict that arise whenever the welfare of one party termed "principal" depends upon actions taken by another party, known as the "agent". The outcome of agency problems is that the principal has to bear costs in order to exercise a control over the performance offered by the agent who having better information is in a more favourable position. The agency costs are faced by the legislator through the "legal strategies" which ultimately have the scope of mitigating the opportunism of the agent and consequently reduce them lowering a heavy burden for the market's players. A good corporate governance model is finalized to facilitate delegated decision-making seen that corporate law is reluctant to confer to shareholders the rights to make decisions. A route-change is in progress in Europe where several directives have been released with the scope of enabling shareholder's empowerment. The last Directive (EU) 2017/828 of the European Parliament and of Council has recently amended a previous one 2007/36/EC always in light of encouragement of long-term shareholder engagement.

Agency problems may often arise during fundamental changes that occur to a company and that can jeopardize the interests of the shareholders and of other stakeholders. Corporate law deals with this kind of changes with the aim of mitigating the opportunism that may appear. When it comes to fundamental changes in corporate charter, crucial differences characterize US and EU systems. US corporate law, in particular the one of Delaware establishes that charter amendments must be proposed only by the board and must be ratified by a majority of outstanding stock. By contrast in European jurisdiction including the U.K. a charter amendment can normally be made by a supermajority of the outstanding stock without the board's initiative. Concerning exceptional operation such as mergers or consolidations the EU faces these situations with the Third Company Law Directive establishing a minimum approval threshold of at least two-thirds of votes at the shareholder's meeting, alternatively one-half of the outstanding votes. It has to be specified that many countries in Europe opt for a stricter discipline requiring higher quorum: Germany and the UK sets out at 75% of voting shareholders while France and Japan need a minimum of two-thirds majority of voting shares with a minimum quorum of one fourth and one-third of the outstanding shares. Concerning the U.S., its law imposes a majority of all outstanding share to approve a merger or fundamental. These requirements are generally applicable for both participants in merger or acquisition. In Europe, shareholder approval is generally for a limited period of time and is necessary for a broader range of decisions than in the U.S.

European shareholders, except in Italy, may also initiate fundamental changes including mergers, major restructurings, by extraordinary resolution, whereas according to Delaware Law shareholder are only endowed with the veto power after that the organic change has been already proposed by the board. Another fundamental difference is that while in the US system the board has the power to issue the stocks, the number of authorized share has to be foreseen by the charter; in EU on the other hand, jurisdiction have set statutory default provisions that pretend shareholder's authorization for the issue of share and pre-emption rights on cash issues. This broader powers of the shareholder's meeting are just a mirror-image of the stronger legal position accorded to the shareholders in Europe if compared with the same in the U.S. America which is characterized by a dispersed ownership and management oriented, the board is the only organ entitled of initiating such modifications limiting shareholder's powers to express, in many cases, in a simple veto power.

This dissertation was inspired by the article named "the case for increasing shareholder power" written by Professor Lucian Bebchuk, where he aims at reconsidering the basic allocation of power between boards and shareholders in publicly traded companies with a widely held ownership. He basically proposes a shareholder empowerment based on evidences that this would entail lower costs of agency and a better management of firms. His article triggered a fruitful and lively debate among scholars in the US where he was harshly contrasted for his idea. The central argument of the Article is that the traditional, director-centered corporate form should be replaced in favor of a novel governance system of Bebchuk's "own invention" — a regime that nominally retains directorial primacy, but in fact eviscerates directorial discretion by vesting directly in shareholders the authority to change the company's charter and authorize mergers and other trans-formative corporate events. The model he proposed, in reality, can be considered as rule-breaking only from a US perspective because it is very close to the framework which already exists since decades in EU.

During the investigation conducted and having analyzed the path covered by the corporate governance of the US, and in EU while shareholder engagement at European meetings remains practically limited, it tends to be well-placed. Shareholders are in fact most likely to act on anti-takeover devices and executive compensation, and submit their own proposals against large and poorly performing firms. Critically, national regulation plays a major role in galvanizing shareholders, lending strong support to the European Commission's Shareholder Rights Directive, and the broader pro-shareholder regulatory trend that has emerged post-crisis worldwide. It came out that shareholders use their voice more at the firm level when concerned about the institutional environment at the country level, and the quality of minority investor protection in particular. Finally it can be said that shareholder engagement at company general meetings is a part of good governance, and regulators should go beyond minimum standards pro-actively to support shareholder rights. A major shareholders engagement in the life of corporations is obviously heavier from a logistic and waste-of-time perspective but is an inevitable burden to bear on the path for good corporate governance. Concerning the US corporate law the recent amendments are in the direction designed by Professor Bebchuk mostly due to the major support pushed by the increasing discontent of the shareholder which strive for more powers

CHAPTER 1

1. INTRODUCTION

The reason why I am writing this dissertation on the role of shareholders in the corporate governance of different countries has to be traced back in the inspiration that I found reading the article written by Professor Lucian Bebchuk and published in the Harvard Law Review in January 2005 which is named "The Case for Increasing Shareholder Power". Reading his article, I fed the interest in conducting a comparison between the corporate governance systems of the most important (in terms of juridical history) European Countries and the American one. Professor Bebchuk is one of the most known worldwide institution of the academic world, who has investigated over corporate topics achieving results that have deeply influenced corporate regulation in the United States and that have received numerous oppositions and supports over the last decade. This article as the professor suggests is aimed at reconsidering the basic allocation of power between boards and shareholders in publicly traded companies with a widely held ownership. Professor Bebchuk looks at the U.S. corporate system proposing changes that are aimed at solving agency problems and enhancing the efficiency of large firms reducing long-lasting problems that have afflicted publicly traded companies.

Bebchuk presents a case for permitting shareholders to initiate and vote in order to choose for changes in the basic corporate governance. Before anticipating the conclusions to Bebchuk's investigation it is necessary to analyze what is meant for corporate governance and what kind of problems are related to it. It follows an analysis of the existing panorama of firm's structures in different countries and the problems strictly related to the governance that the professor tries to solve with the model he proposes.

1.1 CORPORATE GOVERNANCE

Corporate governance is often confused and mixed with the issue of ethics although an ethical behavior is expected from all those actors who take part in the corporate governance process. The real core of corporate governance is represented by the characteristics of a governing process and not about a specific behavioral trait.
Corporate governance occupies one of the most important debate of modern corporate law in particular for listed companies especially after some famous financial scandals such as Enron and Worldcom that have shocked the markets creating the need for major transparency and reliability. Corporate governance has the aim of maintaining and developing effective relationships between the key players in a company (shareholders, the board members, and senior executive management) and other key stakeholders. In order to attain high-performing economies and impartial societies, companies should base these relationships on three essential elements: efficiency, transparency, and accountability. Corporate governance practices are determined by legislation, listing rules, national corporate governance codes, and board decisions[1].

1.2 DEFINITION OF CORPORATE GOVERNANCE

Many definitions of corporate governance have been offered during the past years, and the most significant ones are reported as follows. Corporate governance is the mechanisms, processes and relations by which corporations are controlled and directed.[2]

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[1] A Guide to Corporate Governance in the European Union, International Finance Corporation, World Bank
[2] Shailer, Greg. 2004

Another definition of corporate governance was released from the UK Cadbury Committee in 1992, which described it as “the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders’ role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship”[3]. A following definition was given by the OECD Principles of Corporate Governance (1999) "Corporate governance involves a set of relationships between a company’s management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined" and finally in the year 2011 another definition has been dictated in the “Codice di Autodisciplina” of Borsa Italiana, and is defined as the group of rules by which a company is run and controlled.

1.3 CORPORATE OWNERSHIP

The main goal pursued by the corporate law is the maximization of the aggregate social welfare even if it happens that the legislatures and the courts look with more attention at the interests of influential constituencies, such as controlling shareholders, corporate managers or organized workers. Corporate law everywhere keeps following the historical path through which it has evolved, and reflects a well as the influence of a variety of non-efficiency-oriented intellectual and ideological currents.[4]Among the most developed market economies the number and the nature of corporate shareholders vary considerably

[3] Cadbury Committee Report, *Financial Aspects of Corporate Governance* (1992)
[4] See Mark J.Roe, (2003)
Peter A. Gourevitch and James Shinn, (2005)

and this entail a sign of distinction in corporate law. In common law countries, in particular the U.S. and the UK, there is a vast number of publicly traded companies that have dispersed ownership, which means that no single shareholders or affiliated group of shareholders, is capable of exercising control over the firm.[5] On the contrary in the continental Europe countries, even the public listed companies have traditionally had a controlling shareholder, represented by an individual, a family (Italy), another firm, a closely coordinated group of other firms (as in Germany), or the state (as in France). There is even a great difference among states on the type of entities by or through which the shares are held. In the U.S. for example, the majority of stock are now owned by two types of institutional investors, *mutual funds* and employer established *pension fund* while individuals continue to hold a substantial amount of stocks directly[6]. This situation shows that very rarely individuals are the owners of a large enough share of stock that allow them to exercise control over the company. In Germany, traditionally the major blocks of corporate shares are held by big commercial banks which also serve as custodians for large amount of stock owned by individuals whose rights to vote are often exercised by the banks themselves. In the last years, new types of investor such as *hedge funds and private equity* have appeared to the market and this has entailed numerous changes in the firm's structure, strategy or management[7]. It appears clearly that the corporate law depicts the institutional and political power if country's dominant corporate interests, whether they be banks, prominent families, investment funds or unions. Every country has consciously has shaped its corporate law in order to improve the efficiency with which corporations can be financed and managed in the context of the country's particular pattern of ownership[8].

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[5] Rafaeal La Porta, Florencio Lopez-de-Silananes, Andrei Shleifer, *Corporate Ownership Around the World, 54 Journal of Finance*

[6] Board of Governors of Federal Reserve System, *(2007)*

[7] Brian R. Cheffins and John Armour, *The Eclipse of Private Equity, 33 Delaware Journal of Corporate Law*

[8] Randall K. Morck, *(2005)*

1.4. INFLUENCE OF THE ECONOMIC MODEL ON CORPORATE GOVERNANCE

Corporate governance is deeply influenced by the economic model in use in a determined country; for economic model I mean the relationships and interactions among the economic factors that take part in the process of governance of a company. Two models can be seen as the opposite examples: the German model and the U.S. model. The U.S. one is often characterized as *market-oriented* with more emphasis on “unbridled” competition. The government provides the regulatory framework and lets market forces actors fight it out. The main criteria used is “the winner takes it all” it means that no external forces try to tie the market through interferences. On the other hand, the German model highlights the importance of cooperation and consensus between the different economic market actors and both models present many variations according to the other countries in which they are adopted. In the U.S. the leading state when it comes to corporate law is doubtless Delaware, where many big companies are incorporated and where is established the principle of the primacy of shareholders over the stakeholders[9].

In the EU, on the contrary the law and\or various governance codes, in a majority of states stipulate the primacy of company’s interest i.e. the combined interest of various stakeholders. This main difference between those two frameworks entail broad implications.[10]

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[9] Miguel Mendez, Corporate Governance; a us/eu comparison

[10] See generally Roberta Romano, The Need for Competition in International Securities Regulation, 2 THEORETICAL INQUIRIES L. 387, 516 (2001) (explaining that “network effects of inefficient corporate law provisions (or provisions that lose their efficient properties as business conditions change) will not prevent the emergence of, and switch to, more efficient provisions”); see also Larry E. Ribstein & Bruce H. Kobayashi,

1.5 MODELS OF CORPORATE GOVERNANCE: DUALISTIC AND MONISTIC SYSTEMS

In Europe there are two different board structures that can be used by the companies in order to run their business; the *one-tier* or single board and the *two-tier, vertical or horizontal* systems also known as dual board. This situation of two possible structures is evidently acknowledged by the European Union as it appears clear from the SE governance model which expresses the shared principle at European level.

1.5.1 THE DUALISTIC HORIZONTAL SYSTEM

In our country, the only system of corporate governance that could be adopted by Italian joint stock companies was the dualistic horizontal (or traditional) type; this limitation of choice last until the year 2003. This system is based on the existence of a managing body (sole administrator or, in the collective form of a board of directors) and a controlling organ (board of auditors), which are both organisms that are appointed by the shareholders' assembly. To the board of directors is attributed the duty of directing/managing the company in terms of making the strategic, industrial and financial plans necessary for development, in accordance with the corporate purpose and with the objective of maximizing value for all stakeholders. The essential role of the board of directors is to run the company in compliance with the decisions of the shareholder's assembly. The board of auditors, instead, is appointed to make sure that laws and by-laws are observed, with respect of the principles of good practice as well as the adequacy and functions of the adopted methods of organization, administration and accounting.

Choice of Form and Network Externalities, 43 WM. & MARY L. REV. 79, 128 (2001) (finding that network externalities from legal rules have little impact on the founders' choice of organizational form); Michael J. Whincop, An Empirical Analysis of the Standardisation of Corporate Charter Terms: Opting Out of the Duty of Care, 23 INT'L. REV. L. & ECON. 285, 285-86 (2003) (finding little evidence to support the network externalities argument with respect to Australian charter provisions).

1.5.2 THE DUALISTIC VERTICAL SYSTEM

Taking the inspiration from the German system[11] which has slowly spread to other European countries[12], the dualistic vertical model foresees the distribution of administrative duties to a board of management and the interposition between the board and the assembly of a committee of supervision.

This model therefore entails greater dissociation between owners and management. Regarding the board of management, it does not show any particularities if it is compared to the traditionally composed board of directors, unlike the committee of supervision which presents some peculiar innovative elements being a mixed body of management and control with the functions attributed to the board of auditors, endowed with some specific duties assigned by the assembly and with potential functions of consultancy for the board of management. It is clear then, that with the dualistic vertical model, some of the prerogatives of economic governance initially attributed to the owners are transferred to the supervising committee. The outcome is that, being empowered with both supervisory and managerial powers, it seems wrong to define this body exclusively as a simple organ of control[13]. "This model is perfectly suitable for companies of medium-big size with a widely spread capital or concentrated among professional investors who are

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[11] In this respect it is necessary to point out the existence of some significant elements differing from the German model,
especially concerning the absence, in the Italian dualistic vertical system of:
- an active role of workers and the banks in the committee of supervision;
- powers of authority of the committee of supervision towards the board of management;
- the possibility for the assembly to directly revoke the board of management without having to preventively revoke on the same occasion the whole committee of supervision

[12] This is the case, for example, in France. Elements of evident communion may also be found with the by-laws of the European corporation disciplined by regulation 2157/2001/CE and directive 2001/86/CE.

[13] In effect, they also imply the attribution of powers: supervision and consultancy on the activities of the board of management; effective ex ante supervision; effective ex post supervision

not directly interested in the prerogatives of economic governance, or when the founding partners pass managerial responsibilities to their offspring but still have the possibility of effectively influencing and supervising activities by becoming members of the committee of supervision"[14].

1.6 THE MONISTIC SYSTEM

Getting the inspiration from the model offered by the Anglo-Saxon tradition, the monistic system, compared to the others, is characterized by greater simplicity and flexibility.
The assembly's tasks are the same as those foreseen in the traditional system, exception made for the body of control – unless otherwise stated in the by-laws – which is appointed by the board of directors.

The management of the company is attributed to the board of directors (and cannot be assigned to a sole administrator) formed, for at least one third, by subjects which are embedded with the same prerequisites of independence settled for the auditors or – if contemplated by the company by-laws – those specified by codes of behavior drawn up by trade associations or management companies for regulated markets[15].

A committee is formed to supervise management; this is appointed by the board of director and members are chosen within it. It has the typical functions of the board of auditors and is composed of directors that possess the requisites of honor and professionalism prescribed by the by-laws and the same requisites of independence established for directors.

The allocation of managerial and supervisory functions to a single organism has as a result that this can facilitate the more immediate and deeper knowledge of the management policies adopted or programmed, enhancing the supervision making it faster and more efficient as well as any corrective actions or complaints; but the flipside is that the "controlled" appoints the "controller", with clear contradiction and potential risks in terms

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[14] *International Review of Business Research Papers Vol. 5 No. 1 January 2009*

[15] Art. 2409-septiesdecies, paragraph 1, *Civil Code*.

of effective independence in supervision activities. In the last years, the European panorama, has been a great ground for searching the optimal models of governance which, bearing in mind the existing diversity, leads to the maximum valorization of the company's potential development based on the logic of reliability and transparency. The Italian situation regarding corporate governance highlights the gradually increasing attention on the regulation of governance structures as well as control procedures (internal and external) as a guarantee of the efficient development of activities.

Different analysis carried out in the recent past concerning the structures of corporate governance in the various European countries have stood out some differences among the systems analyzed:

- the models of corporate governance adopted in the different countries;
- the role of share owners and workers with respect to governing bodies;
- the system of appointment among the various corporate organs.

It hast to be emphasized in fact, that in all the industrialized countries (especially for the big joint stock companies quoted on the stock exchange) appeared the need to define rules of governance that allowed the contemporary flow of interests and the cohabitation of every actor that plays a role in the company's life, independently of the degree of involvement of the various players in management.

"In this sense, the whole Europe is witnessing:

- the normative evolution of codes regulating governance bodies;

- the need to strengthen company culture inspired by principles of equality and correct behavior;

- the recovery of company leadership meaning also risk observation and management;

- the growing emphasis of communication processes for the maintenance and growth of consent"[16]

Bearing in mind these considerations, an examination has been made of the corporate

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[16] A. Shirazi and S. Mortazavi 2009

governance structures existing in France, Great Britain, Germany and Spain.
In France the real interventions that brought any changes in corporate on corporate governance were made at the end of 1990s [17] and mainly regulate companies quoted on the exchange.
In particular, modifications consisted in:
- the elimination, in the monistic model, of the obligation to appoint a PDG (Président Directeur Gènèrale) in order to make France more in compliance with the international best practice in particular concerning separation of the chairman's tasks from those of the general manager;
- major powers of control to the board of directors with respect to management;
- a greater transparency of information regarding the remuneration of top management;
- the institution of new supervisory organisms to increase the safeguard of investors;

Corporate governance structures in France are:
- monistic (the chairman of the board of directors cannot also cover the office of general director);
- monistic (the figure of PDG can continue to exist if foreseen in the by laws);
- dualistic (Conseil de surveillance and Directoire).
In the monistic model, the shareholders' assembly appoints the board of directors which, in turn, appoints the Chairman and the General Manager (or the PDG, if the two figures coincide in the same person). In the dualistic model, the shareholders' assembly appoints the control body (and the Chairman), which, in turn, appoints the board of management and designate the Chairman. In both models, an important role is attributed to the workers, in terms of representation in company organs through collaboration with shareholders in preparing the initial list of candidates for the body of control. Great Britain, which is characterized by its Common Law system, although nowadays is only geographically a

[17] For more information on the French self-regulation code, see: R. Vienot dated 1995, R. Vienot dated 1999 and R. Bouton dated 2002. The main legislation concerning corporate governance can be found in Law 420 dated 2001, Law 706 dated 2003 and Law 842 dated 2005

part of Europe has always been and still is more similar to the American system for its Anglo-Saxon traditions than to the civil law system. In effect, the peculiarity of the British system can be found in relation to the active participation of shareholders in corporate governance and the presence of investors in the shareholders' assembly.
The main legislative interventions on corporate governance are traced back to early 1990s[18]. In Great Britain, there is a single corporate organ responsible for running the company business and supervision of activities, has it happens in the United States. This means that, in Great Britain there is a single monistic model of governance, which by its structure foresees the shareholders' assembly appoints to the Board of Directors which in turn appoints the CEO (chief executive officer) among its members. Again even Germany has seen the biggest production on legislation on the subject started in the middle of the last century and intensified in the late 1990s[19]. The greatest innovation was in co-definition at organizational and institutional level but even more important was the valorization of the role of personnel at management level. Workers and investment brokers play a key role in the model of corporate governance adopted and known throughout the world as the "Rhenish model". In effect, in Germany the only governance model foreseen is the dualistic vertical system where the shareholders' assembly and the workers (who, here, have a very important active role in corporate governance) appoint the supervision committee which, in turn, appoints the management committee and is represented by a spokesman. The Rhenish dualistic model differs from the Italian dualistic model because, in German companies, a decisive role is played by the workers and the banks (usually the main shareholders in the companies) in terms of the power to define the composition of the controlling body which, in turn, appoints the board of management. Last but not least, Spain is certainly the country that, more than others, has shown greater resistance to aperture and integration of the various European agreements. The political

[18] Reference is made to the Cadbury Report dated 1992 and later and current Combined Code.
[19] In 1951 a series of laws define company co-determination and co-management. In 1998, the KonTraG entered into force to strengthen the control system and to regulate relations between organs and external information.

and economic background of the nation express why the causes of such phenomena and also the reason why the legislative interventions on corporate governance were done so late if compared to the other jurisdiction examined. It was only at the end of the last century that the first regulations were recorded and even in the recent 2001 the Spanish stock markets were not organized or efficient. We need to wait until 2003 that the Aldama code of self-discipline was introduced revising deeply the contents of the previous Olivencia code, even if the first real reform of corporate governance has been introduced in the late 2006.
Although the various interventions that occurred during those years have not modified or extended the alternative models of corporate governance adoptable in Spain. The only option is the monistic model which remains applicable to joint stock companies in which the shareholders' assembly appoint:
- the board of directors which has managerial and supervisory powers and appoints from within a control committee;
- external auditors.

The Spanish monistic model is much more similar to the Italian monistic model if compare with

British or American ones where, as previously examined, a fundamental role is played by the Board and by the single persons invested with specific roles and responsibilities.

1.7 AGENCY PROBLEMS

As previously specified corporate law has two main functions: fist it establishes the organization of the company and the rules necessary to manage the structure settled; second it has the aim of controlling and solving possible conflicts among corporate actors whether "insiders" such as the controlling shareholders or "outsiders" such as minority shareholders and creditors.
Those kind of conflicts are generally named as "agency problems" or "principal-agent"

problems.

For agency problems is commonly accepted the definition which establishes, the conflict which arise whenever the welfare of one party, termed the “principal” depends upon actions taken by another party, known as the “agent” or according another description the agency dilemma occurs when one person or entity (the "agent") is able to make decisions on behalf of, or that impact, another person or entity, the "principal"[20].

We can say that every relation based on a contract, in which one party promises a performance to another, may potentially suffer from an agency problem.

The difficult situation comes from the fact that the agent has generally better information than does the principal about the relevant facts, this therefore creates a discrepancy in the relation; even more detrimental for the principal is that he cannot easily verify if the performance offered is precisely the one that he was promised. The result of this inequality can be that the agent takes advantage of his stronger position lowering the quality of his performance or even diverting to himself some of what was promised to the principal. As a consequence, the value of the agent’s performance to the principal will be reduced, either directly or because, the principal has to bear the cost of monitoring the agent to assure the quality of his service. The more discretion power must be given to the agent, the higher the cost of agency are going to be[21]. The principal has in fact the need exercising the supervision on the performance undertaken by the agent and this entail an extra economic effort which is possible to reduce through some legal remedies.

1.7.1 THREE GENERIC AGENCY PROBLEMS

In business firms three are most common and easily recognizable agency problems. The first involves the conflict between the firm’s owner and the hired managers. In this case the owners recover the role of the principal whereas the managers are the agents and the

[20] Eisenhardt, K.M. (1989). 57–74

[21] See, e.g., S. Ross, (1973) 134.

conflict may arise because this could be the situation in which the managers pursue their own interests rather than the owners' ones.

The second agency problem concerns the possible dispute that may arise between the controlling (or controlling) shareholders and the minority (or non-controlling) ones. The principal role is represented by the non-controlling shareholders whereas the agent's role is covered by the controlling ones. The problem in this case can show up when a part of the firm' owners can control decisions affecting the class of owners as a whole[22].

The third agency problem concerns the firm itself and the other parties with whom it has contract relations, such as creditors employees and customers and all the remaining stockholders. In this case the firm performs as the agent and so it has not to behave opportunistically such as by exploiting workers, or misleading customers. The problems previously mentioned entail high agency costs that can be mitigated by the use of legal strategies; this would determine benefits for both principals and agents. The reason why lowering the agency costs for principal is obvious but this mechanism would go also in favor of the agents because the principal would be willing to offer a greater compensation for the service if it is assured its quality and honesty. In the previous problems, the difficulty of assuring agents' responsiveness is greater in case of multiple principals who will have to face coordination costs. The outcome is that the coordination costs, will interact with agency problems in two ways:

1. Difficulties of coordination between principals will entail as a direct consequence a major delegation of their decision-making to agents;
2. If it is more difficult for principals to coordinate their own interests, consequently it is more complicated to be sure that the performance of agents will correspond to the one promised.

1.8 LEGAL STRATEGIES

[22] See L. Enriques and P. Volpin, (2007) 117, 122-5.

In order to deal with the agency problems, the law has introduced some *"legal strategies"* which have the aim of mitigating the opportunism of the agents and consequently try to reduce the agency costs that represent a heavy burden for the market's players.

Legal strategies that are adopted with the scope of lowering the agency costs can be divided in two categories; the "regulatory strategies" and the "governance strategies".

The first one establishes the terms that regulate and discipline the relationship between principal-agent, its formation and conclusion tending to constrain the agent's behavior; the second ones increase principal's powers and its control over the agents.[23]

The success or fail of the regulatory strategies depends on different preconditions among which of great importance is the ability of an external authority to verify if the agent has complied with his obligations. On the other hand, in the governance strategies it is required only that the principals themselves are able to observe the actions undertaken by the agent.

1.8.1 REGULATORY STRATEGIES

There are various legal strategies both regulatory; among those ones the *"rules and standard"* and the *"entry and exit terms"* are particularly relevant and both of them try to regulate the substance of agency relationships directly.

The effect of the rules and standard is to constrain the agents by imposing them to not make decisions, or make transactions that would be detrimental for the interests of their principals. In particular the *rules* require or prohibit a specific behavior and the *standards* which leave the precise determination of compliance to adjudicators after the fact. The use of the *rules* is often aimed at protecting the corporation's creditors and is used *ex ante* prescribing a specific behavior to be held. This is why every company's statues embeds *rules* protecting creditors such as dividend restriction or minimum capitalization requirements but at the same time the limits of these tools are evident and cleared by the

[23] An alternative labelling would therefore be a distinction between "agent-constraining" and "principal-empowering" strategies.

fact that very few jurisdictions rely only on the *rules* strategy for regulating intra-corporate relations.

Notwithstanding it is made a wide use of the *rules* in settling the corporate relations, there are some delicate and precise matters that need to be governed by the *standards* rather than rule-based regulation. The standards, being an *ex-post* instrument, leave the precise determination of compliance to adjudicators after the fact have occurred. The real determination of the importance of the rules and standards depends on the way those are enforced; the enforcement of those to instruments in fact is different because if on one hand the rules when well-drafted can be mechanically applied, on the other hand the standards require courts or other adjudicators to be deeply involved in the evaluation and determination of corporate decisions.

As previously anticipated there is a second group of regulatory strategies which aims at regulating the terms and conditions of the relationships between *principal* and *agents* before these are created.

Those strategies are the “terms of entry and exit” which establish the conditions of creation and extinction of the relation between the parties. The law can set the terms of entry which, for instance, impose on the agents the duty to disclose information on the quality of the performance they have promised before even contracting with the principals. An extreme form of the *entry condition is* represented by the need to meet a certain threshold of net worth or financial sophistication in order to be allowed to buy certain securities. The *exit terms* are an ex-post strategy that allows the principal to escape opportunistic agents; among these terms the most common one are the right of withdrawal and the right of transfer.

The first one entails the possibility to retreat the investment made by the principal; an eloquent example is the right of appraisal attributed to the shareholder in case of major transaction such as a merger[24]. The second one is the right of transfer that means the

[24] The withdrawal right is a dominant governance device for the regulation of some non-corporate forms of enterprise such as the common law and partnership a twill, which can be dissolved at any time by any partner. Business corporation sometimes grant similar withdrawal rights to their shareholders through special charter provisions. The most

chance to sell share to the market as expression of the principle of transferability. The transfer rights bring with it possibility of a replacement of the shareholder\principal(s) with a new one that may be more effective in controlling the management of the firm. This right permits also the hostile takeovers thanks to which the shareholders of a bad-run company can sell to a unique buyer that would be much more incline to run the company in an efficient way being highly exposed with his investment.[25]The transfer rights are also prerequisites for stock market, that means a continuous evaluation from the dispersed shareholders which results in the price of the share.

1.9 GOVERNANANCE STRATEGIES

There are six governance strategies that basically depend on the hierarchical elements of the agency relation:

1.9.1 SELECTION AND REMOVAL

The core of this strategy is the power to *select and remove* directors which are pivotal for the control of the enterprise. This is the most direct and efficient way in order to deal with the agency problems first in relation to managers and second in relation to minority shareholders and controlling ones.

1.9.2 INITIATION AND RATIFICATION

This second pair of power give the chance to the principal to have a voice in the management of the company, in particular with these decisions rights they can *initiate or*

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conspicuous example is provided by open-ended investment companies, such as mutual funds in the U.S. which are often formed as business corporations under the general corporation statutes.

[25] Some EU jurisdictions impose limits on the extent to which transfer rights may be impeded.

ratify management's decisions. This strategy is much less efficient if compared with the *selection and removal* because only the most significant corporate decisions need the ratification of the shareholders under existing corporate statutes and generally there is no need for shareholder's initiatives for managerial decisions.

1.9.3 TRUSTEESHIP AND REWARD

This third couple of governance strategies focusses on the incentives for the agents rather than on the expansion of the power of the principals. The *reward* strategy, as the name implies, reward agents for successfully promoting the interest of their principal. In the corporate law there are essentially two reward mechanisms, which are the *sharing rule* and *the pay-for-performance regime*.

The first of these tolls pushes the agent to his best granting to him a monetary return strictly connected to the ones of the principal. The classic example of the sharing rule concerns the equal treatment norm, which entails a pro rata distribution of dividends and as a direct result the controlling shareholders are more willing to maximize the returns of the firm's minority shareholders so that the corporate returns are paid out as dividends.

The second mechanism of this type is the pay-for-performance which couples the interests of the agent with the one of the principal even if not sharing his principal's return.

The trusteeship is the other toll embedded in this family of governance strategies and it is based on the principle of dissolving ex ante any possible conflict of interest so that the agent will not achieve anything from disserving his principal.

This strategy is based on the assumption that lacking the "high powered"[26] monetary incentive to behave opportunistically, agents will respond to the "low powered" incentives

[26] The terms "high powered incentives" and "low powered incentives" are used similarly to the use made in the economic literature pointing the distinction to between the economic incentives on the one hand and ethical or moral incentives on the other. See Bengt Holmstrom and Paul Milgrom, *The Firm as an Incentive System*, 84 American Economic Review 972 (1994).

of conscience, pride and reputation, and are thus more likely to manage in the interest of their principals[27].

All the strategies previously examined which aim at solving the agency problems can be divided in two groups according to the moment in which those are adopted.

Half of it take full effect before the agent acts, whereas the other half are connected to the quality of the agent's performance and so are ex post.

CHAPTER 2

2. SHAREHOLDERS RIGHTS AND INTERESTS

The aim of corporate governance is to facilitate delegated decision-making, and corporate law is reluctant to confer to shareholders the rights to take decision for the company. The European Union has taken seriously then need of a shareholder's empowerment as is explicitly clear from the text of the **Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017** amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement.

"***Article 3c***[28]

[27] . Reinier Kraakman, John Armour, Paul Davies, Luca Enriques, Henry B. Hansmann, Gérard Hertig, Klaus J. Hopt, Hideki Kanda, Edward B. Rock *(2007)42-43*

[28] Directive (EU) 2017/828 EU Parliament**.**

Facilitation of the exercise of shareholder rights

1. Member States shall ensure that the intermediaries facilitate the exercise of the rights by the shareholder, including the right to participate and vote in general meetings, which shall comprise at least one of the following:

(a) the intermediary makes the necessary arrangements for the shareholder or a third party nominated by the shareholder to be able to exercise themselves the rights;

(b) the intermediary exercises the rights flowing from the shares upon the explicit authorization and instruction of the shareholder and for the shareholder's benefit.

2. Member States shall ensure that when votes are cast electronically an electronic confirmation of receipt of the votes is sent to the person that casts the vote.

Member States shall ensure that after the general meeting the shareholder or a third party nominated by the shareholder can obtain, at least upon request, confirmation that their votes have been validly recorded and counted by the company, unless that information is already available to them. Member States may establish a deadline for requesting such confirmation. Such a deadline shall not be longer than three months from the date of the vote.

Where the intermediary receives confirmation as referred to in the first or second subparagraph, it shall transmit it without delay to the shareholder or a third party nominated by the shareholder. Where there is more than one intermediary in the chain of intermediaries the confirmation shall be transmitted between intermediaries without delay, unless the confirmation can be directly transmitted to the shareholder or a third party nominated by the shareholder.

3. The Commission shall be empowered to adopt implementing acts to specify the minimum requirements to facilitate the exercise of shareholder rights laid down in paragraphs 1 and 2 of this Article as regards the types of the facilitation, the format of the electronic confirmation of receipt of the votes, the format for the transmission of the confirmation that the votes have been validly recorded and counted through the chain of intermediaries, including their security and interoperability, and the deadlines to be

complied with. Those implementing acts shall be adopted by 10 September 2018 in accordance with the examination procedure referred to in Article 14a(2)".

The governance costs can be defined as the costs of informing and forging a majority preference among multiple shareholders, as well as the costs of taking mistaken decisions because shareholders are relatively uninformed [29]. Shareholder in fact are empowered of taking decisions principally when directors have conflicted interests or when decisions call for basic changes in governance structure or fundamental transactions that potentially restructure the firm.

Concerning shareholders meeting all jurisdictions permit shareholders to manage directly closely held corporation whereas only some of them allow shareholders to have a direct involvement during operational business decisions in publicly held companies.

Differences appear clearly if we compare the UK, continental Europe, the US and Japan systems.

The UK as a statutory default clause permits to a majority of 75% of the voting shares to sell the company or amend the charter even against the will of the board. In continental Europe and in Japan's jurisdictions a qualified percentage of shares can initiate or approve resolutions on wide range of matters which include fundamental and strategic company directions such as the corporate charter.[30]

On the contrary in the U.S. and in particular in Delaware, which is the American legislation I am mostly focusing on, the law goes as far as possible from the shareholder-centric model. The legislation indeed provides for shareholder's rights to ratify crucial corporate decisions such as mergers and charter amendments but unlike the other countries prevent them from having the power to initiate. Not only US law does not grant the right to initiate but also the range of matter in which shareholder's approval is required is narrower than the one provided by all the others jurisdictions taken into consideration.

[29] H. Hansmann, (1996).

[30] D. Zetzsche, *(2005) 107, 120-8*

A leading example of this difference is represented by the need of shareholder's approval to the distribution of the company's earnings which is present in the German, Italian, Japanese and UK jurisdictions.[31]

The legislations previously examined show also common grounds in same aspects of corporate governance, for example all of them require, or at least recommend companies to have committee structure formed by three parts: audit, compensation and nomination committees. Moreover, all jurisdictions impose a duty of care or prudent management as a legal norm and make use of the norms of disclosure imposed by the market in order to monitor the performance of the public companies.

2.1 MINORITY SHAREHOLDERS

There are different ways in which company law ensure protection to minority shareholders such as by either reserving board seats for the minority or giving an extra weight to their votes in case of election of directors. Being part of the board means the possibility to have access to the information and sometimes to have the chance to form coalitions with the independent directors. Only in Italy minority shareholders have the power to name directors in listed companies whereas in France, the UK, and the US firms can enlist a cumulative voting rule even if it happens rarely but worse in Germany it is still debated if cumulative votes are permissible at all in public companies[32]. Legal tools are used to distribute the appointment powers among the majority and minority shareholders; the best

[31] 58 and 174 AktG (Germany); Art. L.232-12 Code de commerce (France); Art. 2434 Civil Code (Italy); Art. 454(1) Companies Act (Japan); UK law does not prescribe the allocation of the power to approve the distribution of dividends but the model articles require shareholder approval.

[32] Albeit the cumulative voting rule is legally permissble no German large corporation has included this clause in the charter.

known of these instruments is the so called “vote capping”, which is a sort of limit imposed on control rights of large shareholders on one hand, and on the other extending the voting power of the small ones. In respect to this particular device the UK and the U.S. have abolished it by means of listing rules and governance culture, the same result has been achieved in Italy and Germany[33] which have ban it from listed companies and only France still allows publicly traded companies to step for voting caps through a charter provision. In order to protect minority shareholders, the incentive strategy can have two different forms: using the introduction in the board of independent directors and strongly enforcing the fully compliance with the norms of equal treatment among share, specifically concerning distribution of dividends and voting rights. The introduction of independent directors in the board is very commonly used to protect minority shareholders and non-shareholder agents. The premise behind this is that independent directors not having a self-direct interest in the company would deal with controlling shareholders protecting the enterprise in its entirety. This mechanism called the “trusteeship strategy” would reduce the possibility of control of the board by major shareholders of by anyone else.

In order to fulfill the requirement of independence, the director has not to have any family or financial bounds, such as an employment position or consulting relation with the controller. The trusteeship strategy has its pros and cons which are perfectly reflected by the Hollinger case[34] which is relevant because the Delaware Chancery Court sustained the majority of independent directors who excluded a dominant shareholder from the board, and prevented him from exercising is controlling power as he wanted to do. The independent directors however acted only after that the controlling shareholders have committed his moves and after that the SEC had already started the investigation on his misdeeds. Those detrimental acts brought with it that the controlling shareholder had previously broken the contract with the board to promote the sale of the company in all shareholder’s benefit rather than the controller alone.

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[33] Voting caps were abolished in Germany concerning publicly traded companies in 1998.
[34] See Hollinger Int’l, Inc. v. Black, 844 A2d 1022 (Del.Ch 2004).

The second form that the strategy could show is the equal treatment of shares and shareholders of the same class and this binds the controlling shareholders to act in the interest of shareholders as a class which obviously includes the minority too. The U.S., in particular referring to Delaware law, ensures the least equal treatment of identical share among all western jurisdiction, granting the enforcement of the rule only to the payment of dividends. In general, in the U.S. targeted share repurchases, even at prices above the market, are permissible and companies may issue shares to third parties without providing preemption rights to incumbent shareholders. There is another field in which deference to the equal treatment norm has huge consequences and is the law of corporate groups, such

as groups[35] of companies under the common control of another company, often managed as a single business. Some jurisdictions provide for special regulation and the idea behind such regulation is that any single transaction that happens intragroup is part of a wider bunk of transactions that provide offsetting advantages and disadvantages to particular subsidiaries and to the parent company. Subjecting every single transaction within this set to all the controls accorded to related-party transactions in general would needlessly disrupt the group's day to day management. The alternative is then to allow a judicial evaluation of intra-group transactions in aggregate. In Germany for example, the equal treatment norm has wide-ranging application because it has been extended to to aggregates of intra-group transactions: one of the core provisions of formal German group law is the duty of indemnify group subsidiaries for any losses that stem from acting in the group's interests on a yearly basis, which can be viewed as the extrapolation of the equal treatment norm yearly aggregates of transaction. The U.S. corporate law has a different approach in which any particular intra-group transaction between a parent and its partially-owned subsidiaries is subject to the full framework of self-dealing controls. Even Italy and France show different systems from the German one in fact while the first two countries employ a general fairness standard in group law which leaves much to a court's discretion, the

[35] D.P. Forbes and F. J. Milliken, 1999 234-340

German model relies on the more exacting equal treatment norm. However, if this formal difference among those European systems makes a real difference is still uncertain.
There are other remaining strategies for protecting minority shareholders which basically consist in legal constraints, principally in the form of standards such as the duty of loyalty, the oppression standard, and abuse of majority voting. These standards are often specific applications of the equal treatment norm, as when courts allow only fair transactions between companies and their controllers, meaning that in effect that controlling shareholders cannot accept unauthorized distributions form the corporate treasury at the expense of the firm's minority shareholders.

2.2 SHAREHOLDERS VOTES IN RELATED-PARTY TRANSACTIONS

Every single state has introduced different mechanisms in order to subject related-party transactions to legal constraints[36] adopting almost every possible legal strategy with the aim of fighting the agency problems. Every system has made use of one or more of the following tools aiming at solving the problem of related-party transactions: affiliation terms that encompass mandatory disclosure and dissolution rights, agent incentives in the form of trusteeship, decision rights as shareholder approval and agent constraints through rules and standards.
All the major jurisdictions show similarities in addressing the problem of related party transactions; trusteeship, in the form of disinterested or independent director approval, and decisions rights in the form of shareholders meeting approval, with or without counting related-parties' votes are the most widely used. Shareholders' approval is particularly spread in the US and in the U.K. where the so called "majority of the minority" is a well-established institution being two jurisdictions in which large companies lack generally of

[36] Z. Goshen (2003) 91

a controlling shareholder unlike Europe where controlling shareholders have great voting power. There is a wide convergence among all jurisdictions when it is matter of executive compensation; in fact, in every corporate law is required that in the publicly traded companies' directors' compensation is subordinated to shareholder's approval[37].

The European Commission has released a recommendation in which it requires Member States to adopt a legislation so that shareholders of listed companies have the power to influence the remuneration of directors and senior officers. "On 14 December 2004, the Commission adopted Recommendation 2004/913/EC fostering an appropriate regime for the remuneration of directors of listed companies and on 15 February 2005 the Commission adopted Recommendation 2005/162/EC on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. The main objectives of those Recommendations are to ensure transparency of remuneration practices, shareholder control on the remuneration policy and individual remuneration through disclosure and the introduction of a mandatory or advisory vote on the remuneration statement and shareholder approval for share-based remuneration schemes, effective and independent non-executive supervision and at least an advisory role of the remuneration committee with regard to remuneration practices"[38]. Among all the jurisdictions we are discussing about the French and the English ones that are doubtless the most inclined to give shareholders a say in related-party transactions. French law imposes the ratification of the shareholders on all those operations entered during the prior financial year that would fit in the group of "non-routine self-dealing"[39], whereas UK law requires and ex ante authorization from the shareholder for non-routine transactions with directors and large shareholders of listed companies. The other jurisdictions are more

[37] For Italy art 2389 Codice Civile; for Germany 113AktG; for France Art. L 225-45 Code de commerce; for Japna Art 361 Companies Act.

[38] Commission Recommendation of 30 April 2009 complementing Recommendations 2004/913/EC and 2005/162/EC as regards the regime for the remuneration of directors of listed companies.

[39] Art. L.225-40 and 225-88 Code de commerce (France).

lenient on shareholders' approval; Italy for instance requires approval when a director of a publicly-traded corporation aims at sitting on the board of a competing corporation[40]. In Germany the approval of shareholders is required in not listed companies only when the articles of association or the firm's management submit a related party-transaction. There are operations with related-party that are expressly prohibited in some jurisdictions[41]; for instance, loans between the company and one of its directors are forbidden in France and in the U.S. whereas the same operation is allowed in Italy and in UK. Another example of transaction that is subject to restriction is "insider trading" which is generally fought with two sorts of rules: prophylactic restrictions on short-term trading and direct bans on trading on material inside information. The most remarkable rules of the first type are restrictions on "short swing" (less than 6 months) purchase-and-sale or sale-and purchase transactions by statutory insiders of U.S. registered companies including directors, officers, and holders of 10% or more company's equity[42]. The U.K. have adopted the same rules for listed companies while all major jurisdictions have banned insider trading due to nonpublic price-sensitive information about the issuer; moreover, continental Europe have prohibited officers, directors and controlling shareholders of listed companies to trade their companies' securities prior to the disclosure of material nonpublic information[43]. The U.S. extended this ban to all the undisclosed information in "any securities"[44] which means including the ones of the closely held ones. In all jurisdictions controlling shareholders can be held responsible for any unfair self-dealing operations. In the US the risk to be held accountable is higher than in the other systems in the way that courts (in Delaware) apply the entire "fairness test" or the "utmost good faith and loyalty" test (in other state).

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40 Art. 2390 Civil Code.

41 See Stephen M. Bainbridge, (1993) 1034, 1068-81 (describing how judicial review of management buyouts and other conflict of interest transactions focuses on role of independent directors).

42 U.S. 16(b) 1934 Securities Exchange Act.

43 Art. 2 on Market Abuse Directive 2003.

44 Securities Exchange Act 10(b).

Exception made for the US when it comes to face the transactions within the company and its controlling shareholders the jurisdictions tend to have a lighter approach, if compared with transactions between managers and the company, The reason behind this more lenient situation is to be found in the fact that the controlling shareholders generally have much more interest in the company than the managers do being highly exposed with their wealth so that the entails that they are more interested in a long-term performance. Controlling shareholders can exercise their power in appointing the board members and in this way they can influence the affairs of the corporations especially in relation with related-party transactions. Only the US, the U.K. and Japan among the jurisdiction I am taking into consideration show very few widely held listed companies but have a more stringent approach towards controlling shareholders than continental Europe has. The reason behind this lenient approach demonstrated by Italy, France, and Germany is that large shareholders in Europe have exploited their political influence to minimize the regulatory constraint as much as managers have done in the US. In every case ownership regime are dynamic in the way that the higher number of institutional investor ownership around the world and family succession consideration have led to a stricter regulation on related-party transactions in those countries that have underestimated the problem.

2.3 SHAREHOLDERS ROLE IN FUNDAMENTAL CHANGES

Agency problems may often arise in case of fundamental changes that occur to the company and that can jeopardize the interests of the shareholders and of the other stakeholders. Corporate law deals with these kind of changes with the aim of mitigating the opportunism that may appear seen the nature of the situation. As we know the greatest majority of decisions is attributed to the centralized management but this attribution is limited by the importance of the changes that consequently need a broader consensus. Even a board-centered jurisdiction such as Delaware deals with the problems of ensuring protection to the powers attributed to shareholders, to the minority shareholders in order to impede that the majority takes advantage over them, and to creditors that can be fraud by the shareholders. There is no single set of limits of the board's power to decide unilaterally, either across the various jurisdictions or within them, there are only common tendencies. Corporate law generally sets boundaries in board's power when the operation shows at least one of these three following characteristics[45]:1) it has to be a large one if compared to the participant's stake in the company, 2) it is not required particular or technical knowledge to evaluate it, 3) that the operation create a possible conflict of interest for directors, even if it not serious as in case of self-dealing transactions. The reason behind the first characteristic is that the more important is the decision to take, the higher possible has to be the quality of the decisional process. The operation needs to be a sort of investment choice according to the second characteristic and so it does not need any technical knowledge. Even if not serious as the self-dealing transactions, low-power conflicts can still produce detrimental effects to the shareholders and thus need a specific regulation. After a corporation comes into existence with its organizational documents, certificate or articles of incorporation (charter) and bylaws and issues stock, the corporation can subsequently amend those documents as the directors and the shareholders see fit, subject to certain restrictions.

2.4 CHARTER AMENDEMENTS

Corporate law foresees a peculiar regulation for those operations that entail fundamental changes in the **corporate charter[46].** The corporate charter has three main scopes: it declares a specific governance structure chosen, it allows the entrenchment of terms, generally by means of special amendments process, and it is public. Those three main features are common to all the constitutions and unlike the other ordinary contracts can be

[45] Even if generally all these three features are required to be present at the same time.
[46] M. Kahan and E. Rock, *(2003)* 473.

amended with less than unanimity from the parties and are generally available to anyone who asks. The US corporate law, in particular the one of Delaware establishes that charter amendments must be proposed only by the board and must be ratified by a majority of outstanding stock[47]. This provision entail that neither the board nor the shareholders can change the charter without the other party creating the so called bilateral veto; this is a form a guarantee for the shareholders that are not going to see any changes in the charter without their consensus. By contrast in European Jurisdiction, including the U.K., a charter the charter can normally be amended by a super majority of the outstanding stock without the board's initiative.[48] On the other hand, in case of a dispersed ownership, the Delaware system builds a bilateral veto between managers and shareholders, which in this way gives the possibility to the current shareholders to guard against uninformed decision-making by future shareholders at the easing management entrenchment. Both sets of amendments permit corporate planners to entrench governance provisions in the charter; the extent to which corporate provisions entrench rules depends on the structure of share ownership. When shareholders are dispersed, the U.S. corporate law creates a bilateral veto between managers and shareholders, which allow shareholder to guards against uninformed decision-making by future shareholders, at the risk of facilitating management entrenchment. While the U.S. system looks at the bilateral veto as an attractive feature of corporate law, shareholder-centered systems, such as the UK, are more concerned with the management entrenchment, and the charter amendments regime is thus one which formally excludes management from the decision on whether to amend the charter. In a system with concentrated holdings, a bilateral board-shareholder veto is likely to be empty, since controlling shareholders can generally choose boards that will do their bidding. In these frameworks a supermajority voting requirement gives minority shareholders veto, thus creating a bilateral veto among shareholders. In this way the majority can make per-commitments to the minority by means of specific provision that can ensure that their holdings are not diluted below a certain threshold established.

[47] Delaware General Corporation Law.
[48] UK Companies Act 2006, France: Commercial Code, Art. l. 225-96; Germany: Aktiengesetz 199 no 5; Italy: Civil Code, 2365.

Delaware 'corporate[49] law require only a small number of provisions in the charter and leave almost complete discretion with respect to the contents of bylaws[50]. Under both the Model Business Corporation Act and Delaware General Corporation Law as previously specified only the directors can make a proposal to amend the charter and, apart from a few exceptions, there must be express shareholder approval of the proposal for an amendment to be effective, moreover, according to the Delaware statute if a proposed amendment falls under one of three special categories, the most important of which is "adversely" affecting a class (or series) of shares, the affected class (or series) will get to vote on the amendment separately as a class[51]. Concerning the bylaws, The Model Business Corporation Act attributes to both directors and shareholders the power to amend it. In particular articles §10.20(b) gives the power to amend to directors unless (1) the articles of incorporation reserve that power exclusively to the shareholders or (2) the shareholders amend the bylaws in question and stipulate in the bylaw that the director cannot thereafter amend it[52]. For Delaware corporations, the right to amend bylaws

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49 For Delaware corporations, unless expressly prohibited by the charter, the directors can unilaterally change the name of the corporation, delete the names of the incorporators, or delete the provisions that were necessary to effect stock exchange, reclassification, etc., when such changes have become effective. See Delaware General Corporation Law §241(b)(1). See also Model Business Corporation Act §10.05. Furthermore, the charter can grant the right to issue new classes of stock with desired preferences to the directors. See Delaware General Corporation law §102(a)(4). Such a provision is known as the "blank- check preferred" provision.

50 See, e.g., Model Business Corporation Act §10.20 and Delaware General Corporation Law §109. Almost all publicly traded corporations that are incorporated in Delaware have the express provision in their charters granting the right to amend bylaws to the directors.

51 Delaware General Corporation Law §242(b)(2). The other two categories that need a class vote are: (1) changing the number of authorized shares and (2) changing the par value of the stock. Concerning with the changing the number of authorized stock, however, if the original charter or the charter amendment that created the stock so provides, all shareholders can vote as a single class. Next to the section 242, there is another way of amending the charter, through merger ("amendment through merger"). See Delaware General Corporation Law §251(3). Unlike §242(b), however, §251(e) does not mandate a class vote even when a certain class is adversely affected.

52 Model Business Corporation Act. §10.20

belongs to the shareholders but it can be attributed to the directors by means of provision in the charter. Delaware General Corporation Law §109(a) declares that "the power to adopt, amend or repeal bylaws shall be in the stockholders entitled to vote. Notwithstanding the foregoing, any corporation may, in its certificate of incorporation, confer the power to adopt, amend or repeal bylaws upon the directors…[53]". Although the supermajority vote may provide a degree of protection for minorities, most jurisdictions go further by establishing that while charter amendments that adversely separate class of shareholders must be approved by a majority of that class voting together[54].

All jurisdictions generally require corporate charter to deal with some pivotal aspects, in particular in respect of company's shares capital by establishing the number of authorized shares, the number of share classes, their pair values and any restrictions, rights or power on these shares. Delaware law specifies that the while the board has the exclusive power to issue the stocks, the number of authorized share has to be foreseen by the charter. The European jurisdictions on the other hand have statutory default provisions that pretend shareholder's authorization for the issue of shares and pre-emption rights on cash issues. The compulsory matter that have to be dealt with the corporate charter vary from jurisdiction to jurisdiction in particular concerning two aspects. The first one is the structure of the board of directors. In the majority of European countries, the number of board seat (but not the number or function of the board committees) must be indicated by the corporate charter and thus can be amended only through a supermajority shareholder vote. Unlike Europe, in the U.S. those rules are commonly inserted in the bylaws, which contain the provisions for the day-to-day managing of the company, even if those can even

53 See Delaware General Corporation Law §109(a). Amending bylaws is one of the few powers that the shareholders can exercise under Delaware law. The greatest majority of the other "fundamental" changes to the corporation, such as charter amendment, merger, and sale of all or substantially all of the assets, expressly require a board resolution.

54 See. DGCL 242; Art.2376 Civil Code (Italy); Art.L. 225-99 Code de Commerce (France); Companies Act 2006 part 19 ch 9 (UK); AktG 179 (3) (Germany); Art 322 Companies Act (Japan).

be contained in the charter[55] too. Some real detrimental effects can be sustained by the shareholders in case of *issue of new shares;* this operation puts at stake the position of the shareholders that aim at maintaining direct control over major decisions that can jeopardize their interests by diluting their cash flow or voting rights. During the issue of new shares, the managerial opportunism is maximized because this situation can be used in order to build empires, entrench managers and dilute shareholders influence. This delicate operation is faced by almost all jurisdiction by means of requiring the board and shareholder approval. In the U.S. whenever the issue remains below the limit established by the charter no shareholders' approval is necessary and the decisions depends unilaterally on the board. On the contrary if the issue overcomes the threshold sets by the charter the boards 'will is no more sufficient. This rule is surpassed in case of listing corporation when the issue of new share is large enough to entail a shift in voting control over a listed company, unless the new issue takes the form of an offering to dispersed public shareholders.[56] In Europe on the other hand is traditionally required to go through the approval of the shareholders in case of new issue even if it is possible to delegate the that decision to the board, for periods of up to five years[57]. In the case of the opposite operation, which means the *reduction in subscribed legal capital* in publicly held companies must be ratified by a qualified majority of shareholders[58]. On the contrary the U.S. jurisdiction allow companies to have a sufficient discretion concerning their legal capital without any shareholder approval, and this reality represents perfectly the U.S. view of legal capital as old tradition more than a real reason for shareholder's decision rights. Even if all shareholders bear the risk of dilution from new equity and corporate distribution, the worse position is occupied by the minority shareholders because they are not always secured by shareholder decision rights. The protection for the minority comes

55 According to the Delaware law if the charter can be considered as the corporate constitution, the bylaw has to be thought as the corporate statute, and in case of conflict between the charter and the bylaw, the first one has to prevail.
56 See the 312.03(C) NYSE Listed Company Manual and 712, 713 American Stock Exchange Company Guide.
57 Art. 29 Second Directive (now 2012/20/EU).
58 Art. 34 Second Directive.

from the use of toll such as legal strategies. The most representative of sharing norms' example is the preemptive rights which allow the existing shareholders to buy new shares pro rata before that those are offered to the public; in this way this right gives the chance to the minority to safeguard their position in the company and discourage the controlling shareholders from acquiring additional share from the firm at low prices. The U.S. and Japan give application only to those preemptive rights encompassed by the charter through the system of *opt-in* whereas all the other European jurisdiction grant them as statutory default as prescribed by the Second Directive even if European shareholders have the chance to opt out of this default for individual cases through qualified majority[59]. The European preemption has to be enforced only in the case of issue of new shares for cash, whereas in the case of issue of share other-than-in-cash, for public companies the system protects the minority by requiring an independent evaluation. The flipside of the preemptive rights is that they entail a cost in terms of delay of turning to market and so increases the execution risk of new shares; this was clear during the financial crisis of 2008/9 when the need of fresh capital so urgent[60]. This is the reason why both Japan and the U.S. have excluded the preemptive right as default in their corporate charters and have adopted, especially in America, the duty of loyalty which is as effective as preemptive rights are.

2.5 SHAREHOLDERS RIGHTS IN CASE OF MERGERS OR DIVISION

A merger is an agreement that unites two existing companies into one new company. There are several types of mergers and also several reasons why companies carry out mergers. Mergers and acquisitions are commonly done to expand a company's reach, expand into new segments, or gain market share.

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[59] Art.33 of the Second Directive, shareholders must be offered shares on a preemptive basis when the capital increased by consideration in cash, a right cannot be restricted once and for all by corporate charter, but only by general meeting resolution.
[60] See K. Burgess, Financial Times, 3 February 2010.

All of these are done to please shareholders and create value. The importance of mergers is clear because it can bring with it a significant modification in the company's order through revolutionizing the relationships among the participants in the firm. The process of merging can mean the transformation or dilution of the shareholder's ownership's stake.

A shareholder can pass from a position in a widely held company to being part of a controlled firm, or again from being part of a firm with no antitakeover protections to a company with takeover-proof. It can even happen that a member of a publicly held corporation wakes up in a privately held company or vice versa. Being so crucial in the companies' lives, mergers and all the other modes of consolidations receive a strict discipline from all jurisdictions. The capacity of realigning the company's framework entail that mergers have to be treated has being part of the fundamental changes group because they matched the requirements previously stated given that they are large, they often give rise to agency problems, they involve investment-like choices. Determining such big problems almost every jurisdiction impose the supermajority shareholders 'authorization in case of mergers or consolidations. The EU faces these operations with the Third Company Law Directive establishing a minimum approval threshold of at least two-thirds of votes at the shareholder's meeting, alternatively one half of the outstanding votes.[61]It has to be specified that many countries in Europe opt for a stricter discipline

[61] **Directive 2011/35/EU** Art.7:

1. A merger shall require at least the approval of the general meeting of each of the merging companies. The laws of the Member States shall provide that this approval decision shall require a majority of not less than two thirds of the votes attached either to the shares or to the subscribed capital represented.
   The laws of a Member State may, however, provide that a simple majority of the votes specified in the first subparagraph shall be sufficient when at least half of the subscribed capital is represented. Moreover, where appropriate, the rules governing alterations to the memorandum and articles of association shall apply.
2. Where there is more than one class of shares, the decision concerning a merger shall be subject to a separate vote by at least each class of shareholders whose rights are affected by the transaction.

requiring higher quorum: Germany and the UK[62] sets out at 75% of voting shareholders while France and Japan need a minimum of two-thirds majority of voting shares with a minimum quorum of one fourth and one third of the outstanding shares. Concerning the U.S.[63], its law imposes a majority of all outstanding share to approve a merger or fundamental change or the 70% or more of shares that are actually voted. These requirements are generally applicable for both participants in merger or acquisition.

2.6 THE MANAGEMENT-SHAREHOLDER CONFLICTS IN MERGERS

In case of a merger operation there are two principal agency problems that may arise: (a) when managers moved by self-interest refuse to agree to a merger that shareholders instead strive for; and (b) self-interested attempts by management to build empires or to negotiate their future job status or compensation with an acquiring company at the expense of their shareholders. Agency problems are particularly spread in those countries with dispersed ownership such as the U.S.; every jurisdiction addresses the agency conflicts differently; the U.S. in dealing with the eventual resistance of managers to a merger proposal that shareholders are likely to accept uses a mix of trusteeship strategy (board in which is massive the presence of independent directors), reward strategy (high compensation for managers) and an appointment strategy (that gives a chance to shareholders to vote in a new slate of directors in case of veto from the board to a merger). UK discipline on this matter goes parallel with the U.S. even if it differs for two main

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3. The decision shall cover both the approval of the draft terms of merger and any alterations to the memorandum and articles of association necessitated by the merger.

[62] Umwandlungsgesetz (Germany); ss. 899 and 907 of Companies Act 2006 (UK); Arts. L 236-2 and L 225-96 Code de commerce (France).
[63] 11.04 (e) RMBCA.

points: the lack of board veto, there less difficulty in removing directors. Concerning the second agency problems that occurs in case of a merger when managers put their personal interests before the one of shareholders, the disciplines dictated in the various jurisdictions are pretty similar. Shareholders' approval is a mechanism able to challenge a merger inclined by managers. Sometimes it is possible to form coalition of shareholders which represent a block big enough to stop actions so that a better alternative transaction can be undergone by the company.[64] In the UE the law establishes the need of gatekeepers'(independent experts) approval of the merger's terms when it comes to public companies whereas in the U.S. public companies in order to avoid suits from the shareholders try to receive the endorsement on the operation from the banks. Another tool used by Japan and U.S. corporate law is the exit strategy that grant to the unhappy shareholders to avoid the financial effects of the fundamental changes approved by the majority of shareholders by selling their share at a fair price given the circumstances[65].
In Italy the law provides for a similar instrument grants appraisal rights to shareholders of closed companies and to those of listed ones in case of merger with a non-listed company.[66] The appraisal rights are granted by French and German corporate law in particular when a merger determines the change in the legal form or introduces any unusual restrictions on shareholder's rights. The appraisal rights find limits in Delaware and RMBCA jurisdictions by means of the so-called "stock market exception"; under this exception shareholders do not receive appraisal right if the merger consideration consists of stock in widely held company rather than cash, debt, or closely held equity, apparently on the theory either that appraisal rights ought to protect the liquidity rather than the value of minority shares, or that the valuation provided by the market, while imperfect, is unlikely to be systematically less accurate than that provided by a court. This also explains why the European Jurisdictions have never adopted the exit strategy as the general remedy

[64] See M. Kahan and E. (2007) 1021.
[65] On the appraisal remedy under Japanese law, look at Alan K. Koh, Appraising Japan's Appraisal Remedy, 62 American Journal of Comparative Law 417 (2014).
[66] Civil code, art. 2505-IV (closed companies) and 2437-V (listed into non-listed companies).

to protect minority shareholders in mergers but instead adopted trusteeship and decision rights strategies requiring the valuation made by independent experts who are held accountable for their unlawful conduct[67]. Not only European countries have to respect the minimum guarantees granted imposed by EU laws but some of them go beyond granting to individual shareholders [68]the rights to criticize the fairness of the merger prices. Among those jurisdictions, Germany and Italy, in particular provide to the shareholders for the possibility to sue the new company formed for the discrepancy between the value of the shares they previously owned and the value of those received after the operation was over and this system has proved to be so effective that in those countries has acted ad deterrent to mergers.

2.6.1 THE MAJORITY–MINORITY SHAREHOLDER CONFLICT IN MERGERS

In case of presence of a controlling shareholder, mergers with unconnected companies involve risks for minority shareholders and for this reason some of the instruments (such as appraisal rights or independent expert assessment) previously introduced used for limiting manager-shareholder conflicts are often adopted with the same aim of reducing the disputes between majority and minority shareholders. The conflict between majority and minority is particular severe in freeze-out mergers where a controlling shareholder,

[67] Art. 20 Third Directive (liability of managers towards their shareholders) and Art. 21 (liability of independent experts towards shareholders).

[68] 15 Umwandlungsgesetz; Art. 2504-IV Civil Code; see also Karsten Schmidt, Gesellwschaftsrecht 390 (4th edn, 2002); Pierre-Henri Conac, Luca Enriques, and Martin Gelter, Constraining Dominant Shareholders' Self-Dealing; The Legal Framework in France, Germany, Italy, 4 European Company and Financial Law Review(2007) 491, 525.

using the merger operation, gets rid of the non-controlling shareholders either for cash or stock[69]. European jurisdictions offer minority shareholders protection through a variety of standards in case of related party transactions; Franch law, for example, establishes that mergers can be invalidated under the *abuse de majorité*[70] doctrine, whereas in the UK the "unfair prejudice" remedy is at least potentially available to provide an exit right for the minority at a fair price. In the US the standards play a relatively small role in the regulation of most arm's-length fundamental changes (except when the company is broken up or a merger or other transactions promises to create a new controlling shareholders where had been none before)[71], they become prominent in controlling shareholder's transactions.[72]Jurisdictions generally provide for minority buyouts when a controlling shareholder owns more than 90 percent of a company's shares. EU instead lets member states to exchange the appraisal rights for expert's evaluations of the merger operation and to dispense with the need for a vote by the shareholders of the acquiring company- which is an alternative that takes inspiration form the Germany s'*Konzernrecht.*[73]In the U.S. a parent company that owns more than 90 % of the subsidiary can unilaterally merge the subsidiary into itself without any consultation with the shareholders meeting but only granting the appraisal rights.

U.S. laws allow cash-out mergers, or as they are said the freeze-outs, in situations in which the controlling shareholders own less than 90 percent of a subsidiary's shares.

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[69] See M. Venturozzo. (2010) 841

[71] See e.g. Paramount Communications, Inc. Atlantic Reporter 2d 34 (Delaware Supreme Court 1994).

[72] See Mahoney and Weinstein, note 103,272-4; compare Weinberger v UOP, Inc.,457 Atlantic Reporter 2d 701 (Delaware Supreme Court 1983); *Kahn v.Iynch Communication systems, Inc*. 638 Atlantic Reporter 2d 1111 (Delaware 1994). Robert B Thompson, *Squeeze-out and the "New" Appraisal Remedy*, 62 Washington University Law Quaterly 415 (1984).

[73] See Arts. 27-29 Third Directive. See also Volker Emmerich and Mathias Habersack, Konzernrecht 141-6 (10th edn., 2013).

U.S. securities regulation requires public corporations that go private, (as result of a freeze-out merger), to make any disclosure regarding the fairness of the transaction and to any eventual third parties that could find any interest in the acquisition of the company.[74]The courts in Delaware generally analyze the parent-subsidiary mergers under the strict criteria of "entire fairness" standard, with the burden on the controlling shareholder to demonstrate the fair price and fair process. However, the burden of proof is shifted to the plaintiff where the transaction was either (i) negotiated by a special committee comprised of independent directors or (ii)supplemented by the majority of minority shareholders. When both these steps are taken, the transaction will be reviewed in light of the business judgment rule[75]. A different discipline is dictated by European law which sets out a more neutral approach if compared to the U.S. one in relation with freeze-outs, not facilitating the operations and establishing only minimum requirements through the Directives. In France, a company's charter may provide that its minority shareholders can be cashed-out in well-defined circumstances, although the terms of such a buy-out would be subject to a sort of Delaware fairness review by the courts. On the other hand, German law recognizes the rights of a controlling shareholder to free-out an abusive minority shareholder, but neither the German statutes nor the German courts acknowledge a general right of controlling shareholders with under 95% of an issuer's shares to freeze out its minority shareholders[76]. In Italy no right to cash out minorities is foreseen by corporate law, a freeze-out can happen only in case of shareholders with a number of shares lower than it is needed to receive one share in the resulting company[77].

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[74] Rule 13e-3 1934 Secuirities Exchange Act.

[75] *Kahn v. M F Worldwide Corp*. 88 Atlantic Reporter 3 365; see also *In re Cox Communications,* Inc. 879 Atlantic Reporter 2d 604. See Chapter 6.2.2.1.

[76] BGH, March 20, 1995-II ZR 205/94, BGHZ 129, 136

[77] See L. Bianchi (2002) 101.

2.6.2 FREEZE-OUT THROUGH NON-MERGER TECHNIQUES

Many jurisdictions provide also squeeze-out techniques which are not based formally on a merger transaction. EU law in fact establishes that if an acquirer ends up with 90 to 95 % of the target's shares after a public offer than, as a consequence, is able to freeze-out the non-accepting shareholders on the basis of a public offer and the minority has an equivalent righto be bought out. In France a shareholder group which has 95 percent or more of voting rights in a listed company may eliminate the minority by making a public offer to acquire their shares, followed by a mandatory acquisition of the shares of the non-accepting shareholders[78]. The value to be paid in the compulsory acquisition has to be approved ex ante by the market regulator, which operates on the ground of a proposal prepared by the acquirer's investment bank, the report of an expert commissioned by the target and its own judgment.[79] In Germany too the law provides for a squeeze-out procedure at the 95 percent level for all public companies, which track merger rules (including the need for a report from the 95% shareholder and a report form a court-appointed expert on the adequacy of the compensation).[80] Unlike to what happens in the French system the price is not approved ex ante but instead it has to be challenged by minority before a court whose decision will apply to all minority shareholders. Even if the challenge does not normally imply any suspension to the immediate effect of the squeeze-out, the procedure can be protracted (even up to 10 years), generating an incentive for the 95 percent shareholder to settle the minority's claim and an equally strong incentive for arbitrageurs to acquire the minority's shares in order to take advantage of the court challenge.

In the U.K. there is a lack of procedures for squeezing out minorities (other than post bid) and so a variety of more broad corporate schemes can be used. One of these basic

[78] Art. L. 433-4 Code Monetaire et Financier; Arts.236-3, 236-4, and 237-1 Règlement General de l'AMF. The minority has a parellel right to be bought out (Art. L. 433-4 Code Monetaire et Financier; Arts 236-1 and 236-2 Reglement General de l'AMF).

[79] Arts. 237-2, 261-1 (II), and 262-1 Reglement General de l'AMF.

[80] 327°-f AktG. See Thomas Stohlmeier. German Public Takeover Law 139.

mechanisms is a charter amendment requiring the minority to transfer their share to the minority or to the company. Being possible that the standard supermajority requirement for charter amendments is deemed inadequate for minority protection in squeeze-out situation, UK courts under their general power to review charter changes[81], have developed a requirement for a good corporate reason for even a fair-price squeeze-out, in contrast with the basic requirement for good faith in respect of other changes to the charter.

2.7 CORPORATE DIVISIONS

The division of a company is directly the inverse operation of a merger; the scope of the division is the separation of the assets and liabilities of a single corporation into two or more surviving corporations, one of which can be the dividing corporation itself.[82] The U.S. only regulates divisions on an ad hoc basis when opportunisms appears or when the company sells all or substantially all of its assets. Even if the rules contained in the Sixth Company Law Directive[83] regulating divisions are a virtual mirror-image of the Third Directive dealing with mergers, including its provisions on minority and creditor protection, practically instead, member stare do not scrutinize divisions as closely as merger, and then the fulfillment of all those requirements can be avoided. Even when the division rules find application, European shareholders are less protected than they are in the inverse operation of merger. The reason behind this discrepancy can be found in the fact that a division has a different impact on the company itself, because it merely restructures the existing assets and liabilities of a company instead of adding to the company's existing assets and liabilities. Moreover, even more significant is the less risk

[81] See Gamlestaden Fastigheter AB v. Baltic Partners Ltd (2008) BCLC 468
[82] The division of a company has to be clearly distinguished from the creation of a subsidiary; while in the latter case it is also the case that a corporation divides into two entities, in the former case, the divided entity does not end up holding the shares in the newly formed company or issued by another company in exchange for the company's assets.
[83] Sixth Company Law Directive 82/891/EEC, 1982 O.J. (L 378) 47.

of conflict of interests in a corporate division than in a merger, at least concerning managers and shareholders. Other stakeholder can be damaged from a division in particular creditors and employees. The risk is that creditor’ claims will not be satisfied because the division of assets and liabilities, which is decided in the division contract, is not pro rata as between the receiving companies. This is why the EU corporate law introduced a system by which making the companies receiving the assets jointly and severally accountable to pre-divisions creditors; the liability of the receiving companies other than the one to which the debt was transferred may be limited to the value of the assets transferred.[84]

2.8 REINCORPORATION

The migration of a corporation between jurisdictions can drastically mutate the relationship among the participants. If the corporate law in the new seat is more pro-management or pro-controlling shareholders this can obviously worsen the relationships aggravating the agency problems; on the other hand if the new home's law is less protective with non-shareholders' parties the migration can be a mean by which shareholders and managers transfer value from non-shareholder constituencies to themselves. Corporate migration can happen through various mechanisms; in Canada, for instance, a company can move its jurisdiction and at the same time keeping legal personality (all its legal rights and obligations) between provinces, requiring two-thirds votes of shareholders, as long as the corporate body will, inter alia, remain liable to creditors in the new jurisdiction.[85]

A more common system used in order to migrate is the merger; in the U.S. for example, if a Texas corporation wants to move to Delaware generally merges with a newly

[84] Art. 12 Sixth Directive.

[85] D. Cumming and J. MacIntosh (2002) 277, 279.

established wholly owned Delaware subsidiary, with the Delaware subsidiary continuing as the surviving corporation. Normally if the migration is made throughout a merger the minority shareholders and the other constituencies are as protected as they are during a normal merger. The new shareholders of the Delaware corporation receive the same percentage of shares that owned in the previous Texas company.

Another mechanism that requires a shareholder vote and court approval is used elsewhere in order to give effect to the migration.[86]EU has recently supported the cross-border mobility within Europe with the aim of increasing the spread of standard schemes in corporate law and has done it by using three main paths to effect a relocation within member states countries.

The first way to reincorporate in another EU jurisdiction is by converting into the equivalent legal form of the destination state, relying on the case-law of the European Court of Justice. On this matter *Cartesio*[87] and *Vale*[88] are two leading decisions of the ECJ thanks to which is now clear that a member state has to offer the conversion procedure for accommodating foreign companies, similar to its local laws, and that the state of origin is under the same corresponding obligation to allow the company to leave.[89]

Another possible strategy is to use a Societas Europaea as legal form, which is a European company entity that expressly permits cross-border relocation with retention of legal personality.[90]

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[86] J G. Hill, (2010) 63

[87] Case C-210/06Cartesio Oktatò és Szolgàltatò bt, (2008) ECR I-9641.

[88] Case C-378/10 Vale Èpitesi kft, ECLI:EU:C:2012:440.

[90] SE Regulation, Arts 8,8 and 69. The only downside is that a reincorporation also requires a simultaneous shift in the location of its head office. See Wolf-Georg Ringe, The European Company Statute in the Context of Freedom of Establishment, 7 Journal of Corporate Law
Studies 185 (2007).

Creditors employees and minority shareholders are protected by art 8 of the SE Regulation which attributes them a system of protection rights. [91]

The third route for corporate migration is to employ the European Cross-Border Merger Directive[92], which offers a system similar to the one of the U.S. and so the migration of the company through a merger with an existing or a newly formed company or subsidiary in the destination state. But unlike the U.S., the Directive provides for a series of protections for shareholders, creditors, and employees in addition to those foreseen for domestic mergers. One concern may arise in particular with respect to the protection of the employees in case the reincorporation is made in a jurisdiction that is less caring with board representation of the employees. Both the SE and the CBM Directive face this problem establishing the principle that the pre-reincorporation rules will continue to apply post-reincorporation. According to this principle when one or more companies that are merging or forming an SE are subject to employees board-level influence requirements, those requirements will be carried over the surviving or resulting company, even if the laws of the new state of incorporation would not otherwise require board-level influence.[93] This rules dictated by the European Law are meant to be strong and this becomes clear because for amending these provisions both managers and employee representative have to negotiate a different solution in advance of the reincorporation.[94] This system aims at preventing cross-border merger form undermining existing board-level voice

[91] Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE), Art 8, par 5. " A Member State may, in the case of SEs registered within its territory, adopt provisions designed to ensure appropriate protection for minority shareholders who oppose a transfer".

[92] Directive 2005/56/EC of October 2005 on the cross-border merger of limited liability companies, 2005 O.J. jumped the gun by holding in the SEVIC case that Germany violated Arts. 49 and 56 TFEU (freedom of establishment and capital by permitting the registration of domestic mergers without also permitting equivalent registration of cross-border mergers (Case C-411/03 SEVIC System AG)

[93] Wolf-Georg Ringe, Mitbestummungsrechtliche Folgen einer SE-sitzverlrgung, Neue Zeitschrift Fur Gesellschaftsrecht 931 (2006).

[94] P. Devis, (2003)

requirements but not to extend such requirements to companies not previously subject to them. In Germany however, corporations have been over-represented in the number of SEs formed to date and seem to have been able to achieve what they regard as attractive modifications of their national employee representation systems, even if they have been unable to avoid codetermination altogether.[95]

2.9 CONVERSION

Firms can also opt for changing the type of corporate form or abandon the form altogether in favor of partial corporate forms or other organizational structures making then the *conversion.* As for the migration, the outcome of a conversion is a wholesale alteration in the default and mandatory rules provided by law. Delaware law requires an exceptionally strong decision strategy to police conversions being the only corporate decisions which need the unanimous shareholder approval.[96] Many jurisdictions treat the conversion as any other charter amendments basing the discipline on a combination of decision strategies in the form of supermajority voting requirements and on judicial enforcement of fiduciary duties,[97] even if the quorum required to approve a conversion may also depend on the new entity type being selected and on the nature of its different model. US law requires the approval of a majority of the outstanding shares for a merger leading to a conversion into a limited liability company, but of two-thirds of the outstanding share for a conversion or merger into a public benefit corporation- an organizational form which, which aims at pursuing public benefits beyond profits.[98]

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[95] See B. Keller and F. Werner, (2008).
[96] DGCL 266.
[97] Umwandlungsgesetz 226, 240 (Germany) and CA 2006, section 90 (UK), both need a 75 percent majority requirement for conversion from private to public company.
[98] DGCL 363.

2.10 FUNDAMENTAL CHANGES AND REGULATION

As noted in the previous paragraphs almost every jurisdiction converges on the treatment of fundamental corporate changes in the distinction between the group of corporate actions that are completely delegated to the board, and the tiny bulk of corporate changes in which instead the board's authority is limited by a shareholder's vote requirement or direct regulation. Fundamental changes are often constrained by a decision rights strategy whereas other complementary strategies seem to be rarer. In all western jurisdictions merger, charter amendments, reincorporation, and dissolution fall outside the scope or delegation to the board of directors, and require shareholder approval, usually with a special quorum. Albeit there is a general common ground in facing this kind of corporate changes among jurisdictions, there are some differences which are not purely related to the division between common and civil law. Continental Europe jurisdictions make less use of the judicial enforced standards to regulate mergers than the Anglo-American jurisdictions do. France and Germany rely as heavily on standards as the U.S. or the UK do.

Generally, we can say that the EU focuses more attention to the management-shareholder conflicts in regulating corporate decisions than does the law of U.S. jurisdictions. In Europe, shareholder approval is generally for a limited period of time and is necessary for a broader range of decisions than in the U.S.

European shareholders, except in Italy, may also initiate fundamental changes including mergers, major restructurings, by extraordinary resolution, whereas in American jurisdictions shareholder are only endowed with the veto power after that the organic change has been already proposed by the board. This broader powers of the shareholder's meeting are just a mirror-image of the stronger legal position accorded to the shareholders in Europe if compared with the same in the U.S. America which is characterized by a dispersed ownership and management oriented, the board is the only organ entitled of initiating such modifications. We have to say that if the U.S system, on one hand, provides for less protection to the shareholders as a class, on the other hand, it offers more protection to minority shareholders by means of exit strategy, in the form of appraisal rights for minority who vote against merger or other organic transactions, or by providing the standard of fairness, backed by the threat of a class action lawsuit, for pivotal transactions between entities controlled by a dominant shareholder. On the other hand, European boards do not limit the power of controlling shareholder being appraisal rights unusual in EU and shareholder facing enforcement difficulties if they want to claim a violation of standards. The differences among the principal systems can be found also in the kind of strategies that for the common law countries are generally adopted *ex-post* whereas for continental Europe are more *ex-ante.*

CHAPTER 3

3.1 BEBCHUCK'S PROPOSED REGIME: THE CASE FOR INCREASING SHAREHOLDER POWERS

As I have anticipated in the introduction, the previous paragraphs were necessary for understanding the regimes that Professor Bebchuk proposed in his article. Corporate governance shows differences among the different jurisdictions and in particular between civil law countries and common law one. The aim of this dissertation is not to decide which is the best model to adopt but instead to create a clear mirror of the existing situations and being aware of the current problems related to corporate governance; moreover, the researchers previously debated want to enable an evaluation regarding the system proposed by Bebchuk which he strives to be adopted by the American jurisdiction. Personally, I find the regime the proposes a positive innovation for the US corporate governance system and I am strongly convinced by the arguments he brings to sustain his thesis.

According to the ideas that he depicts in the article the modification to the U.S. discipline should entail the power for shareholders to initiate and vote on a proposal regarding certain particular corporate decisions.
US corporate law is characterized by the fundamental principle that all major corporate decisions must come from the initiation of the board whereas shareholders can only to adopt a corporate decision by replacing incumbent directors with new ones that are supposed to make the change for which they have been appointed.[99]

[99] See Robert Charles Clark, Corporate Law (1986) 21-24, 93-140.

The implications of this framework are evident and according to the article, the kind of powers that Bebchuck would consider to attribute to shareholders are limited to two different groups of corporate decisions. The first is known as "the rules of the game" decisions to modify the corporate charter or to change the state where the company is incorporated. The second group regards those business decisions which are particularly relevant and that can be divided into two subcategories: the "game ending" decisions, which include mergers, the sale of all the assets of the company or dissolve the company, and the "scaling-down" decisions which are means by which diminishing the size of the company through cash or in-kind distribution. One of the pivotal principles that govern the U.S. and UK corporate governance is that shareholders don't have the power to impose to the directors to follow any particular course of action, but rather they can exercise their powers within the limits set by the corporate statutes and by the company's constitutional documents.[100] Even if this prescription of the two systems is similar their corporate codes shows big differences one to each other in the treatment of shareholder intervention. When referring to U.S. discipline in the corporate governance the system established is the one settled the Model Business Corporation Act (MBCA) which were adopted by the Delaware state is then followed by other 24 U.S. states[101]. As previously exposed According to Bebchuck the board of directors has the control over three categories of decision: rules-of-the-game decisions, game-ending decisions, and scaling-down decisions.

3.2 RULES-OF-THE-GAME

The first group consists of all the choices of the rules by which corporate actors play that are determined by the corporate charter and by the laws of the company's state of incorporation. Both the charter and the state of incorporation can be changed even if such

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[100] See Paramaount Communications, Inc. v Time, Inc., 571 A.2d 1140,1154 (Del.1989); Charlestown Boot & Shoe Co. V. Dunsmore, 60 N.H. 85, 87 (1880); Automatic Self-cleansing Filter Syndicate Co.V. Cuninghame (1906) Ch. 34,43 (Eng. C.A. 1906).
[101] Model Business Corporate Act.

changes generally require the initiation of the managers. According to Delaware's code and the MBCA in fact, any charter modification must be proposed by the board and must be brought under shareholder's approval. No matter the number of shareholders that aim at carrying out a charter amendment shareholders cannot vote on it unless the board chooses to have such a vote. Shareholders also lack the power bring any changes to the state where the company is incorporated. There is no state statute that offers explicitly the chance to reincorporate the company in a different state and as I have mentioned in the previous paragraphs, most of the time the reincorporation is done through mergers with corporations located in the state where the companies want to move. Being the merger the most common system used for the migration of the company, the discipline of the merger applies including the rule that such operation can be initiated by the board. Shareholders, on the other hand, have the chance to amend company's bylaws which is the act that can regulate some aspects of the corporate governance.[102] The bylaw even if is crucial for the company’s day-lives is subordinate to the charter and cannot bring any alteration to the framework imposed by it[103]; moreover, only the charter is able to opt out of various provisions of the Delaware Code and the MBCA.[104]

Bebchuk suggests the bylaw should have a broader scope by providing a full account of the benefits that result from shareholder power to make rule-of-the-game decisions, but given that some changes can be made only through charter provisions and not using the bylaw, the benefits of letting shareholder make rules-of-the-game decisions could be fully accomplished only allowing them to carry out amendments to the charter. The professor claims instead of letting shareholder initiate "second-order-rules" in the form of bylaw provisions while denying them the chance to initiate first-order-rules in the form of charter provision is an inconsistency that should be resolved in the sense of allowing the

[102] See Delaware Code Ann. Tit 8, 109, Model Business. Corp. Act. 10.20.

[103] The Delaware General Corporation Law limits authorized bylaws to provisions “not inconsistent with…. the certificate of incorporation” Del. Code Ann. Tit 8, 109(b). The MBCA limits bylaws to provision “not inconsistent with the… articles of incorporation” MBCA 2.06 (b)

[104] See Del Ann. Tit. 8, 102 (b)(i), 141 (a).

shareholder to initiate not only bylaws provision but also all other rules-of-the-game. Is noteworthy to specify that shareholder are endowed with the power to express their will in favor of given charter amendment or reincorporation using the precatory proposal[105], which by the way is a non-binding instrument. Following the state corporate law directors are able to continue the path designed by the shareholders or deny to follow the proposal being sure to be protected by the business judgment rule[106].

3.3 SPECIFIC BUSINESS DECISIONS: GAME ENDING and SCALING DOWN

As we know in the system settled out by the Delaware Code and by the MBCA, all the major operations, such as mergers, consolidations, the sale of all assets, and dissolution require the approval by a majority of the outstanding shares and are part of the so-called "game-ending-decisions". To the shareholder on this aspect is attributed only a veto power which means the substantial lack of power to give rise to such decisions whereas the board is the only organ entitled to bring such decisions.

Delaware corporate law establishes the board has to determine the distributions either in cash or in kind without any need to receive the approval from the shareholder. Distributions are seen as part of the ordinary conduct of business attributed to the management and for this reason, unlike the game-ending decisions, the shareholders are not endowed with the veto power. Courts have even denied their competence to review the decisions of the management specifying that these operations fall under the business judgment rule.

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105 See Louis Loss & Joel Seligman, Fundamental of Securities Regulation 550-73.
106 Cf. Spiegel v Buntrock, 571 A.2d 767, 775-76 (Del 1900).

Bebchuk after this analysis on the allocation of power between management and shareholders in the U.S. focuses his attention on the different approach showed by the United Kingdom. Like in the American system in the U.K. the framework is set by the statute, the memorandum and the articles of association. The statute establishes that any eventual changes in the memorandum or to the articles of association can be made by "special resolution" that require a supermajority approval of 75% of the votes of the cast at the shareholder's meeting[107]. The memorandum or the articles of association cannot eliminate or limit the power to change these basic documents by special resolution[108]. Shareholders in the U.K. are entitled to bring to a shareholder vote special resolutions to change the memorandum or articles of association, they have the right to propose such amendments to the annual shareholder meeting provided that the notice was properly given. Furthermore, shareholders that possess at least the ten percent of the company's shares can call a special meeting and therefore propose the amendments in that occasion. The UK system sets that the board is subject to "any direction given by the special resolution" of the shareholder's[109], even more decisive is that the memorandum of understanding and the articles of association can be changed by a special resolution and can also impose a different set of division of power between the board and the shareholders. Shareholders are even always capable of replacing all the director at any time with a majority of votes cast in a special meeting invoked for this purpose. It comes with, Bebchuck says, that notwithstanding both the U.K. and the US remiges belong those same common law system, a shareholder in the United Kingdom enjoys greater powers and a greater influence over the board.

3.4 SHAREHOLDERS SHOULD SET THE RULES

[107] Companies Act, 1985, c. 6. Halsbury's statutes of England and Wales 88, 112, 432.
[108] See Malleson v. Nat'l Ins. & Guar. Corp., (1894)
[109] Company Act app, at tbl. A, art 70.

The quality of corporate governance can exercise a deep influence over the firm's performance and shareholders. In the publicly held companies, the interests of shareholders and the ones of the managers do not always fully match. The result of this discrepancy is that agency costs arise and this, as we know, is faced thorough legal strategies. , on the other hand, suggests that in order to maximize company's value defeating the agency costs, shareholders should be able to initiate and adopt rule-of-the-game decisions to amend the charter or to reincorporate in another state.

The professor highlights the limits of the shareholders ‘power to replace director; as he explains that “one could argue that the power to replace directors is sufficient to ensure that the value-enhancing changes in governance arrangements will occur even if shareholders lack the power to initiate them”.[110] This way of reasoning proceeds stating that, seen that managers know that if they do not follow the indication of the shareholders they can be replaced, they would generally not neglect shareholders interest and vice versa shareholders would not need to replace the board. To wrap up then, even if incumbent directors are not often replaced, shareholder's power to replace exercise a persuasive force over the management to carry out a value-increasing change in rules, thus creating no need for shareholders to have the power to make rules of the game decisions. Bebchuk in his article goes expressly against these ideas offering an explanation of why shareholder power to replace directors cannot secure rules-of-the-game decisions that would be value-increasing and does so by using as an example the precatory resolution to dismantle staggered boards. According to the statistics in fact, the presence of a staggered board in a company sees, as a result, the high probability that the targets of a hostile bid remain independent, and this entails that there is a reduction of the returns for target’s shareholders both in the short-run and in the long-run.[111]Moreover, according to the professor, there is evidence that staggered board is strictly related to low firm value[112]This

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[110] Lucian Bebchuk, 2005 pag 85

[111] See L. Bebchuk, C. Coates IV & G. Subramanian, July 2003); see L Bebchuk, John C. Coates IV & G. Subramanian 887, 925-39 (2002); L. Bebchuk, John C. Coates IV & G. Subramanian, 906-08 (2002).

[112]See L. Bebchuk & Alma Cohen, *The Costs of Entrenched Boards*.

means that directors of a company where shareholders have approved a precatory resolution to repeal a staggered board cannot sustain that shareholder's will is inconsistent or irrational seen the evidences.

Bebchuk focuses his attention on this simple question: has management followed majority passed resolutions to repeal staggered boards?[113] The statistics he reports in his article concern an analysis conducted on companies in which shareholders have passed a resolution to repeal staggered boards during 1997-2003. The evidences show that by more than 2\3 of the resolutions that have achieved the majority consensus during the period 1997-2003 were not implemented by the board by fall 2004. This data depicts a situation in which directors did not follow the indication given by the majority of shareholders even if those precatory resolutions passed more than once. The evidences that the professor brings as argument in his article make clear that the cases in which management do not follow majority passed resolution to repeal staggered boards represent the greatest majority and furthermore show as the existing power to remove director is not per se sufficient to guarantee that manager would initiate any changes in the governance framework in order to increase shareholder's value. The power of shareholders to replace director finds substantial impediments,[114] challengers, in fact, don't enjoy access to the ballot and to the corporation's proxy machinery that instead incumbent can exploit. Another big obstacle for challengers is represented by the costs that they have to bear by themselves whereas incumbents are financed by the company. Bebchuk claims that according to researchers that he has conducted in a seven-year period 1996-2002 among thousands of public companies, there were only 11 challenges every year and this number falls till two when it comes to firms with more than $200 millions of capitalization. This is why he suggests changes in the corporate elections process in order to make shareholder's power effective and really viable. The professor adds that even if such reforms enter into force, this wouldn't be enough for eliminating the need for shareholder power to make-rules-of-the-game decisions. The vote that conduces to the replacement of

[113] L. Bebchuk, 2005 page 854.

[114] L Bebchuk,.*2003 pag 43, 44-46, 64-66* .

the incumbent directors with a new team that promises to initiate such a given rules-of-the-game change is not the perfect tool for attaining the aimed change. Such a vote wraps together (i) the given change in rules and (ii) and the replacement of incumbent director with the rival team.
Bebchuk analyses than the veto power entitled to the shareholders in respect of the charter amendments and reincorporation proposed by management. Similarly to what happens with the power to replace directors, someone could claim that this veto power can ensure that decisions regarding basic governance framework are made in the interest of the shareholder in order to increase their value. Bebchuk is of total contrary opinion; the veto power, in fact, is a tool that enables shareholders to impede that detrimental decisions for their interests are undertaken by the management. It is a very different instrument from the power to initiate rule changes, and it is a "negative" power that precludes any worsening of the of the shareholder's situation. Being a passive form of protection it cannot provide any increase in shareholder's value ad it cannot obtain any change that favors shareholder's interests. There is no guarantee that shareholder's veto power ensures a value-maximizing outcome even in the case in which there are potential changes that would make both shareholders and the directors better of relative to the status quo. In this case, in fact, if it is true that the change would benefit the shareholders too, it is also true that it could not be the change that maximizes shareholder's interests.

Bebchuk offers as an example the case in which there are three possible charter amendments X, Y, and Z that would, as a consequence, favor both shareholders and managers if compared with the status quo. Among the three possible options of charter amendments, X is the choice would maximize shareholder's value followed by Y and Z. On the other hand, if we take into consideration management's interests the order is opposite; so Z, Y, and X. The veto power that shareholders enjoy won't enable them to select option X; X would not be selected even in a hypothetical situation in which both managers and shareholders have to agree to a change and each side can suggest a proposal to the other. In this situation, the parties would be symmetrically situated showing the same opportunity to exercise an influence on the selection. This hypothetical case would likely bring to the Y arrangement which satisfy equally both sides and which represents the second-best choice for each of the two parts. This situation, however, is not the one existing under current U.S. corporate law because shareholders and directors do not enjoy the same powers. Managers do not have the sole veto power but they can brag the power to propose changes which is something that shareholders cannot do. This means that being a monopolistic system in respect to the initiation of changes; in the example that the professor has proposed, this entails the directors which have stronger bargaining position, are much more inclined to choose option Z which maximizes their interests. At same time option Z represents an improvement for shareholders even if it is only the weaker one among the other possible choices. A similar example could be made concerning reincorporation; whenever a company wants to reincorporate in a more favorable state, and different states are at stake, the choices proposed by managers is likely to be the one that favors them the most although it represents always an improvement for shareholders too.

Managers could exploit their superior bargaining power even in the case that they want shareholders to approve a change that would entail a decrease in shareholder's value. In fact, they can manage to bring shareholder to vote for a negative change using tactics given by their position. The directors can include the negative change in a second positive transaction that could bring benefits to shareholders. In this way, shareholders that initially were not willing to vote for a negative change would now approve an operation where the improvements overlap the negative aspects.

Bebchuk claims that shareholders must be able to initiate and adopt any rules-of-the-game decisions in particular concerning both corporate charters changes and changes in the state where the company is incorporated. To support his ideas, the professor analyzes the current corporate situation; the companies operate in a dynamic environment and this means that the optimal set of corporate governance framework needs to vary from time to time according to the new problems that may arise. The control that managers exercise over the charter amendments is inclined to realize changes in management's favor.

Eventual changes that would increase shareholder's value will not be adopted if they make management worse off, and more as previously said if there is a change that can better off both shareholders and managers, the change that will be undergone is likely to be the one that best serves the shareholders. According to Bebchuk this the problem of pro-management distortions in the charter amendment process should be faced by a corporate law in a way that counters these distortions. He suggests the use of mandatory rules that could make up for shareholder's inability to rely on charter amendments process to produce value-maximizing charter amendments in midstream companies[115]. The professor claims that mandatory rules are desirable but however but hardly can eliminate these distortions and can only reduce the adverse consequences of the pro-management bias in the charter amendment process. Instead, when shareholders are able to initiate changes they will be able to value-increasing changes that management does not favor for its own reasons. Regarding the reincorporation, Bebchuck explains how attributing the power of making the rules-of-the-game decisions would bring with it a direct improvement in the corporate law rules of the states among which companies may choose to incorporate, creating a sort of competition among jurisdictions for offering the better system able to increase shareholder's value. The results of this positive competition would led to changes for a better corporate law for publicly traded companies, and a better set of arrangements aimed at increasing shareholder 'value. A reform that guarantees to shareholder the power to adopt rules-of-the-game decisions would lessen the need for other corporate law reforms. As the professor says, once the constitutional change is made, shareholders will have "self-help" tools to address governance flaws, and outsiders (public officials) will have less need to intervene. With this constitutional change shareholder's intervention could effectively contribute to solve all those governance problems that can eventually arise.[116]

[115] See Bebchuk, 1820-25; see also N. Gordon, (1989),1577-80.
[116] See e.g. Frank H. Easterbrook & Daniel R. Fishel, The economic Structure of Corporate Law, ch. 1 (1991); Frank H. Easterbrook & Daniel R. Fishel, The Corporate Contract, 89 Colum. L. Rev 1416 (1989).

3.5 BEBCHUK'S REFORM

The model sustained by Bebchuck is the outcome of an evaluation that comprehends not many different possible solutions. He took into consideration every aspect that could matter in terms of preciseness of the model proposed; (i) first of all he addressed the problem of when and how often shareholders should be able to initiate proposals for the rules-of-the-game decisions. Under his proposal shareholders would be able to submit such proposals for consideration in any annual meeting or not only in annual meeting but also in special meetings as is possible in the U.K. (ii) Second he dealt with the holding and ownership requirements establishing that in his suggested regime only shareholders or group of shareholders that reach certain specific thresholds should be permitted to submit proposals. He defines the threshold as modest but at the same time not as low as the minimum requirement for precatory resolutions. (iii) Third indicates that the regime he proposes would not permit the submission of a proposal to a shareholder vote when an equivalent proposal was recently strongly denied. Its provisions have the aim of impeding losing time and money for proposals that are very unlikely to receive the majority necessary to pass. (IV) In the regime that Bebchuck proposes when shareholders submit a proposal to amend the charter or reincorporate then it is allowed the submission of counter-proposals. This chance to bring counter-proposals will lead to a panorama where shareholders will have more options on the table and this will entail a higher probability for the shareholder to choose the best system in terms of shareholder's value. He adds to this regime that seems reasonable to confer to directors the power to have the prerogative for the "last proposal", which consists in the right to add, after the passage of the deadline for the submission of proposals by the shareholders to be voted on in a given meeting, with a new proposal to be voted on at the same meeting.

(V) Under the current rules, a management-initiated proposal will be adopted if and only if it receives a majority of the votes in one meeting. In order to suffocate all the concerns regarding this shareholder power to intervene, the requirements for approval of shareholder-initiated changes could be designed as able to guarantee that not only the proposal receives the approval at some given time but that it shows a constant, and lasting support. Under the regime that Bebchuck has foreseen a proposal would be adopted if it only receives shareholder approval in two subsequent annual meetings. The vote in the first meeting can be seen as a vote to schedule the real decisive vote in the subsequent meeting. The idea proposed by the professor has the aim of facing two types of concerns that could arise with shareholder's intervention power. This method, in fact, may reduce the potential costs from nuisance proposals; with this strategy management would be little distracted by proposals that are unlikely to attain shareholder's consensus and also it addresses the concerns over rule changed motivated by short-term interests or preferences of some shareholders. With this requirement, it is safe that a proposal would be approved only if it enjoys the same support after a significant period of time. The current rules establish that a management-initiate change needs support from the majority of the outstanding shares to be adopted, this is why the professor sees as fair to set the same threshold for shareholder-initiated proposals. He also claims that it would be desirable to require firms to reimburse reasonable expenses to shareholders that have launched a proposal which receives a certain threshold of success[117]. This prevision could alleviate the problems that arise when a shareholder that bring a desirable proposal has to bear all the costs and enjoy only a part of the benefits given by the change itself.

Bebchuk in his article specifies that the legislative intervention should be made at a federal level which, according to him, could introduce directly a power to make rules-of-the-game decisions or could alternatively require the states of the union to amend their corporate law so as to attribute this power. This legislative innovation would have as an additional result an improvement of the firm's selections among any given menu of state law choices and as a consequence a competition among states to offer the best solution for shareholders[118]. Concerning the possibility to opt-out from the scheme designed, the

[117] See Lucian Arye Bebchuk & Marcel Kahan, *A framework for Analyzing Legal Policy Towards Proxy Contests*, 78 Cal. L. Rev. 1071, 1085-87 (1990).

[118] ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW (1993). See also

professor clarifies that this debate goes beyond the scope of his article but adds that he would limit the contractual freedom in corporate law[119].

3.6 BEBCHUK'S ANALYSIS OF POSSIBLE OBJECTIONS TO HIS REFORM

Professor Bebchuk in his article does not limit the analysis of the topic to the reasons of his reforms but goes further studying the possible oppositions and critics that he may receive after the publication of the article. A possible objection of providing to the shareholder with the power to initiate changes in basic rules is that this power would hardly translate in the adoption of shareholder-proposed changes. He thinks that two opposition could be: (1) shareholders would not have any incentive to initiate such proposals, and (2) that proposals that are initiated are unlikely to obtain majority approval. His response is that both those to proposition are unfounded because with his reforms the majority of the benefits would result in inducing management to initiate desirable changes and thus it would not matter the frequency with which shareholder-initiated proposals are actually adopted.

3.6.1 THE BURDEN OF THE COSTS OF USELESS PROPOSALS

Another problem that may arise concerns the costs that the companies and the shareholder would bear in case of a proposal initiated by the shareholders which have very low chances

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William J. Carney, The Political Economy of Competition for Corporate Charters, 26 J. LEGAL STUD. 303 (1997) (discussing the advantages of competitive federalism in producing efficient laws).

[119] L. Bebchuck, 2005, 1404-08; and see L. Bebchuk, 152 (2003).

to receive the necessary support. Bebchuk has already explained how the regime more than really be based on shareholder's proposal would entail that the management starts changes by itself; but still, one could argue that many shareholders might bring proposals that have poor chance to pass because they are, ill-considered, implausible, or induced by motivation other than shareholder wealth. Even if this kind of proposals will not pass in the vote produce a cost that the company will have to bear: shareholders would have to express a negative opinion and the director would spend money, time and attention in trying to conduct a campaign against them.[120]The idea proposed by Bebchuck comprehends the need to maintain acceptable costs for the "nuisance proposal". He has designed the threshold requirement necessary for the proposal submission by a shareholder or a group of shareholders and this means that the company would not lose time over meaningless or frivolous proposals. Another form of guarantee in order to avoid useless proposals is the process of screening that the proposal that impedes to vote on proposals that are similar to previous proposals that didn't obtain the necessary threshold in the previous year.[121]

The proposals that meet the requirement for the submission but that enjoy a poor support among shareholders, with difficulty can generate significant inconvenience for either shareholder or management. shareholders won't face any inconvenience till shareholder's

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[120] This concern is similar to the one expressed by supporters of management insulation withrespect to the shareholder access proposal. M. Lipton & S. A. Rosenblum, (2003),67.

[121] Requirements of this sort are already used in connection with the initiation of votes on precatory resolutions. See, e.g., LOSS & SELIGMAN, supra note 26, at 569–72. However, because the goal of votes on precatory resolutions is to air issues rather than produce binding outcomes, current securities laws allow resubmission of resolutions as long as they exceedsome very low threshold of support in preceding votes.

In contrast, because the proposed regime seeks to facilitate actual rule changes when desirable, there would be little point in allowing a revote on a proposal that, for example, received five percent of the votes in thepreceding annual election.

Finally, it is worth noting that if it is desirable to further reduce the extent to which management and shareholders might be distracted, this objective can be served by concentrating
all voting on shareholder-initiated proposals at the annual meeting.

proposals need a majority of outstanding shares approval, as opposed to a majority of the shares that take part in a vote. Being that abstaining is equivalent to voting against, shareholders that are not willing to vote in favor of a proposal don't need to bother voting against. Concerning the inconvenience that proposals can create to management, the problematic situation is avoided because only if a proposal receives the majority in the first meeting managers (that do not support the proposal) would be compelled to lobby against. So as Bebchuck says, "managers thanks to the two-successive-meeting requirement" would have a safety net"[122].

3.6.2 SHAREHOLDER WHO MAKE WRONG DECISIONS

The professor has assumed that in the regime he has designed shareholder would adopt changes that necessary bring as effect an increase in shareholder's value; but what if the changes proposed has not the positive effect desired? Bebchuk analyses the situation in which shareholders might support a change that has detrimental effects to the long-term share value, due to (i) they don't have the right information, (ii) their interventions might entail a cost in term of discrepancies with the decision taken by the management, (iii) they can be driven by short-term consideration or special interests.

1)IMPERFECT INFORMATION

The wrong information problem that can influence the choices of the shareholders is considered the most common issue against the expansion of shareholder's right; this is due to the position they have which very often is seen as having an informational disadvantage in respect of managers. They are likely to have insufficient information unlike managers, or either have poor incentives to obtain and evaluate all available public information[123]. Corporate law has long accepted the view that management might

[122] L Bebchuk, 2005, pag 880.

[123] Shareholders bear the costs of obtaining and assessing information but do not capture

sometimes have better information[124], and being better informed it comes with it that it is more likely to choose the best arrangement for enhancing shareholder's value. As a consequence, if the directors take the rules-of-the-game decisions shareholders are protected by erroneous possible choices[125]. However rules-of-the-game decisions do not turn on inside, company-specific information. Taking for instance, the decisions whether to amend the charter to remove a staggered board or whether to reincorporate the company in Delaware. Institutional investors encounter these questions in many companies, and the answers to such questions are often based on judgments concerning issues that arise in a wide range of companies. Albeit individuals can reasonably disagree on how to answer these questions, the answers to them are unlikely to depend on inside information that management has but that shareholders lack.

Even more significant, even if it were the case that management sometimes is better informed than shareholders about which rules-of-the-game decision would better satisfy shareholder interests, management would not have the best incentives for adopting the right decisions. Management might prefer to avoid a charter amendment that would enhance shareholders value but that would also restrict its freedom or limits its private benefits. It is clear then, not attributing the power to adopt rules of the game decisions to the shareholders, this would remain to the management that even if can rely on better information is surely less motivated. Attributing the power to intervene to the shareholder implies that whatever better information the directors could have will not influence the choices of the governance framework. In the regime proposed by Bebchuck, the management will recommend to the shareholder on the intervention thanks to the better knowledge that it has. Shareholder will then evaluate the better information that directors have and that they might be driven by self-serving reason. Once balanced those two

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the full benefits that result from more informed voting decisions. See Bebchuk, Limiting Contractual Freedom in Corporate Law, supra note 72, at 1836–40.

[124] See, e.g., Paramount Communications, Inc. v. Time, Inc., Fed. Sec. L. Rep. (CCH) 94,514, 93,277 (Del. Ch. 1989) (“No one, after all, has access to more information concerning the corporation’s present and future condition [than managers].”).

[125] See, e.g., Jeffrey N. Gordon, 347, 353–55 (1991); M. Lipton, 101, 115–16 (1979).

contrasting elements, a rational shareholder might often conclude that deference would be best on an expected-value basis. Other times, however, they could think differently and reach the opposite conclusion. Even if shareholders try to do their best, they can commit mistakes on the evaluation but always being highly motivated to best serve their own interests[126]. On the other hand, in a regime in which shareholders are precluded from starting a change, deference to management is mandated as a general rule. The choice of regime, then, does not depend on whether shareholders are better informed than management, but rather on whether shareholders should be able to decide the degree of deference that will be given to management's recommendations.

2) THE INCONSISTENCY PROBLEM

Another issue that could arise and potentially weakening Bebchuck's proposal is the inconsistency coming from shareholders' decisions that would lack coherence with management's corporate decisions.

One could argue that there are certain corporate governance issues that should not be answered in isolation from how other corporate decisions are made. According to this argument, the shareholders should have a secondary role, or as is commonly said, "sit calmly in the back seat and not to try to instruct the person the wheel" because any interference might entail any accidents or at least to a nerve-racking trip. This consistency argument is not sufficiently strong to provide a good ground for refusing

[126] Note that in deciding whether to defer, shareholders will be in the same situation as many parties who must decide whether to defer to an agent who has greater expertise but worse incentives. Because we expect self-interested individuals to have incentives to balance
the costs and benefits of deference, we generally believe that such parties would be better off if they were permitted to decide for themselves instead of being required to defer to the expert agent. Few would support mandating that clients defer to the recommendation of their lawyers when deciding whether to accept a settlement offer.

shareholder power to make rules-of-the-game-decisions.
In fact, in many cases, the regime proposed with the new governance rules would be consistent with management's business policy, and in this situation, there is no point in giving management a veto over the choice of governance rule. Management's choice of business strategy does not require that its choice be decisive with respect to questions such as whether all directors should stand up for elections annually or whether stock options should be expensed. Moreover, the argument against back-seat driving is affected by the same problem as the argument about imperfect information: the shareholders themselves could and should decide how much weight to give to the consistency consideration. Attributing the power to make decisions does not mean that shareholders would continuously take decisions but rather they might defer to management when they think that a consistency in decision-making is necessary.
To sum up, as for the other contrary arguments, the inconsistency problem is not strong enough to impede the adoption of this shareholder empowerment regime. Back-seat driving could sometimes be inconsistent with the decisions taken by the management but this eventual situation is not per se sufficient to discourage the adoption of this change.

3) SPECIAL INTERESTS AND SHORT-TERM HORIZONS

Another critic that could be moved against shareholders initiated proposals concerns the possibility that shareholders might be motivated by consideration other than long-term shares value. There are some shareholders, such as financial institutions, that having high turnover strategies, might aim at achieving short-term stock prices and consequently might produce changes that would be detrimental to long-term value and to long-term shareholders. This critic, however, does not find any support because even if some shareholders are moved by short-term interests the changes in corporate governance provisions initiated by shareholder cannot be adopted without receiving the consensus of

the majority of the outstanding shares. It follows then, that a proposal that pursues special interests or an activist agenda at the expense of shareholder value would have no meaningful chance of obtaining the majority support. This conclusion is supported by the example of precatory resolutions which systematically obtain the majority support only when are viewed as value-enhancing by a large range of financial institutions- such as de-staggering the board or rescinding poison pills. On the other hand, proposals that are focused on social or special interest issues uniformly fall far short of a majority.
If the arguments sustaining shareholder's empowerment regime are not considered sufficient and so it remains a concern about proposals that would have positive short-term effects but negative long-term effects, it is possible to design a regime of shareholder intervention power in a way that would address this concern. In particular, a shareholder intervention regime could be designed to enable shareholder-initiated proposals to become valid only after a significant time from when they are brought. Under the regime suggested a proposal won't become valid until after the passage of two shareholder's meetings, held at least one year apart. Thanks to this provision, shareholders will be able to initiate and finally adopt proposals only if they think after one year from the beginning of the process that the change would have beneficial effects in the long term.

3.7 OPPORTUNISTIC PROPOSAL

It could be argued that permitting shareholders to intervene would enable some of them to bring proposals simply in an effort to extract some personal benefits from the directors. So if this is the premise it comes with it that union pension funds could leverage their initiation power to extract concessions for labor[127]. Whereas some other large shareholder

[127] See John J. Castellani & Amy L. Goodman,pag 77 (2004).

could use their initiation power to acquire financial or other benefits from management[128]. Analyzing this potential concern, it becomes evident that management wouldn't be particularly worried by the possible "blackmail" consisting in a threat to bring proposals for a change that would likely be value-decreasing, given the unlikelihood to obtain the majority support. It is worth noting to consider the possibility of shareholders' blackmailing management by threatening to introduce a proposal that management recognizes to be value-increasing and thus likely to gain majority support. The potential for blackmail in such a case would be limited by the fact that striking a deal with the blackmailer would not prevent the proposal from being initiated.

The article written by Harvard's professor has a characteristically provocative theme, *The Case for Increasing Shareholder Power*, and has stimulated lively and fruitful debate in the pages of the *Review* and beyond. There have been many answers to his article which in part supported his ideas and in part contrasted the regime he proposed. I am now analyzing those comments that more than others are able to threaten the validity of his proposal and which are then worth of being mentioned.
Theodore N. Mirvis, Paul K. Rowe, & William Savitt, have cooperated with the aim of responding to Bebchuk'article showing its weaknesses and unfeasibility.[129]
According to their ideas, Bebchuk's proposal overthrow the core Delaware corporate law principles risking extraordinarily costly disruption without any assurance of the corresponding benefit; they claim that Bebchuk's case is unsupported by any persuasive

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[128] See Stephen J. Choi & Andrew T. Guzman, Choice and Federal Intervention in Corporate961, 987 (2001) (expressing concern that large block shareholders may act opportunistically and "threaten to initiate a campaign to shift to [a regime that reduces overall
share value] unless management 'pays off' the block shareholder"); Gordon, supra note 99, at 383–84 (expressing a similar concern).
[129] Theodore N. Mirvis, Paul K. Rowe, and William Savitt are partners at Wachtell, Lipton, Rosen & Katz in New York who specialize in corporate and Mergers & Acquisitions-related litigation. Theodore N. Mirvis and Paul K. Rowe are members of the board of advisors of the Harvard Law School Program on Corporate Governance.

empirical data; they sustain that Bebchuk's premise that corporate boards cannot be trusted to respect their fiduciary duty has no reason to exist in the observed experience of boardroom practitioners.

As we know the basic argument of his article is the traditional director-centered corporate form should be replaced in favor of the governance system that Bebchuck proposes which explicitly retains directorial primacy, and eviscerates management discretion by attributing directly to shareholder the authority to change the company's charter and authorize transformative corporate events.[130] Theodore N. Mirvis, Paul K. Rowe, & William Savitt start their opposition by reporting Vice Chancellor Strine's "corporate law traditionalist" opinion, that Bebchuk's approach would undermine "the core element of the Delaware way: the empowerment of centralized management to make and pursue risky business decisions through diverse means.[131]" Those authors criticize the Bebchuk revolutionary idea by simply supporting the US corporate governance status quo, which according to them has had an enormous historical success of the Delaware approach.

They move principally three objections which according to my personal view do not find any reason and are not able to contrast the idea proposed by Bebchuk.

The first critic is that his regime reverses Delaware corporate principles and therefore risking extraordinary costly disruption without any assurance of the corresponding benefit. Secondly, they object Bebchuk's proposal which sustains that corporate boards cannot be trusted to respect their fiduciary duties - finding no resonance in the observed experience of boardroom practitioners. And as third objection, proposal of the professor exalts shareholder power in a way that is inconsistent with statute and years of Delaware case law but also is particularly suspect in light of the palpable practical problems of any shareholder-centric approach.

1) The first critic is based on the pivotal principle that the "business and affairs" of

[130] Lucian Bebchuk,pag 833 (2005).

[131] Leo Strine, Jr., *(2006)*1759, 1763.

every Delaware corporation "shall be managed by or under the direction of a board of directors." This simple statement of board primacy, which appears as Section 141(a) of the Delaware General Corporation Law, announces a general principle that is reflected in the Delaware statute and case law. Accordingly, the Delaware model "invests corporate managers with a great deal of authority to pursue business strategies through diverse means, subject to a few important constraints." As Bainbridge in his separate reply puts it, Bebchuk wishes "to replace the existing, mostly permissive rules disempowering shareholders with a new set of mostly mandatory rules empowering them." And Vice Chancellor Strine's "traditionalist" observes that Bebchuk aims at nothing less than the replacement of the traditional corporate republic with a form of direct shareholder democracy. The authors claim that is impossible to predict the result of the regime proposed[132], and also that raises complex issues relating to the allocation of risk and reward between shareholders and corporations. As a general rule, the organ entrusted with the corporate management bears the legal risk for the action of their corporation. On the other hand, with this new regime shareholder would take the benefits of corporate performance without having the risk of liability for harm that the corporation may cause to others. My personal answers to these critics are that even if it is not possible to predict how corporations would respond to this change of asset because the history of US corporate governance lacks kind of experience, a sort of similar framework to the one proposed can be seen at work in the European Union jurisdictions. Concerning the second objection of the legal risk; if it true that shareholder would not bear the personal responsibility directly, it is also true that the company itself would respond and consequently the shareholders

[132] Recent scholarship confirms the risk that "shareholder empowerment" may yield deleterious unintended consequences. For example, Lynn Stout observes that so-called "shareholder democracy" appears to be encouraging private buy-outs of public companies, concluding that "[t]here is reason to suspect that the modern trend toward greater 'shareholder power' has gone too far and is beginning to harm the very shareholders it was designed to protect." Lynn Stout, *Investors Who Are Too Bolshy For Their Own Good*, FIN. TIMES, Apr. 23, 2007 at 9.

indirectly.

2) The second objection that authors move in respect to *The Case for Increasing Shareholder Power* is that it assumes as almost certain that directors do not seek to advance shareholder interest but are to the contrary engaged in a constant struggle to extract private benefits at shareholders' expense. We are thus treated to arguments built on the hypothesis that "for self-serving reasons, management does not wish to initiate value-increasing change[s]," and asked to entertain fanciful models of the "bargaining" that takes place between directors on the one hand and shareholders on the other, in which directors' "monopoly" over corporate policy allows them to avoid value-enhancing policies and endorse politics that go in their personal favor. They claim that these arguments brought by Bebchuk find no evidence in reality. Advisors who work with public company directors know that directors are aware of their fiduciary duties to shareholders and to the other stakeholders in general and express their role by advising on how to satisfy those duties and are vigilant to find and solve potential a conflicts[133]. Albeit the critics moved against Bebchuk's regime I support his point when he states that shareholder should be entrusted with the power to initiate changes in order to defeat the agency costs. Agency costs are the reason why many corporate

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[133] *See* Robert K. Rasmussen & Douglas G. Baird, *The Prime Directive* 3–4 (Vanderbilt Univ. Law Sch., Law & Economics Working Paper No. 06-19, 2006) (criticizing scholarly focus on agency costs as excessive and for detracting from the board's "prime directive" of choosing the best managers); Stout, *supra* note 8, at 1436. In a similar vein, the late Sumantra Ghoshal persuasively argued that the "agency model" remains paramount in corporate governance research, notwithstanding the evident reality "that companies survive and prosper when they simultaneously pay attention to the interests of customers, employees, shareholders, and perhaps even the communities in which they operate," largely due to the scholarly preference for "testable propositions" and "reductionist prescriptions" over "the wisdom of common sense." *See* Martin Lipton, *Twenty-Five Years After* Takeover Bids in the Target's Boardroom*: Old Battles, New Attacks, and the Continuing War*, 60 BUS. LAW. 1369, 1379 (2005) (quoting Sumantra Ghoshal, *Bad Management Theories Are Destroying Good Management Practices*, 4 ACAD. OF MGMT. LEARNING & EDUC. 75, 81 (2005)).

governance issues arise and even if his ideas of the “selfish-management” could be seen as exaggerated or too pessimistic, in a way that directors cannot be trusted, why should US firms even have a small percentage of risk that their managers pursue their own interests, rather than shareholders and company’s ones?

3) The third critic that is raised from Bebchuk's opponents is that the shareholder-centric thesis is based on the premise that shareholders are pushed by the shared objective of maximizing share value and that shareholders will use their power to achieve the common goal of higher share value. It follows with this premise that if a shareholder has private interests diverse from the other shareholders, that particular shareholder should be expected to use its vote to advance its agenda, possibly to the damage of the other shareholders or corporation generally.[134]

   This objection, by the way, does not seem to be sufficiently strong to impede the adoption of the regime proposed. In fact, if on one hand it could be possible that a shareholder is advancing his private interests with detriment of the others shareholders, on the other hand is also true that that a proposal that pursues a special interests or an activist agenda at the expense of shareholder value would have no meaningful chance of obtaining the majority support. Even more persuasive is that the proposal needs to receive the majority in a double vote year from the other. To sum up then, I believe that neither one of this critics has minimally weakened the arguments brought by professor Bebchuk, but even more have clarified how strong his points are.

3.8 THE CASE FOR EMPOWERING US SHAREHOLDER

[134] Unlike directors, shareholders (other than controlling shareholders) do not owe fiduciary duties to other shareholders, are not otherwise obligated to advance the best interests of the firm, and are not subject to any of the other legal, social or reputational constraints that govern board conduct. Thus, it is reasonable to expect shareholders to promote their private interests in the same circumstances where experience shows directors will act for the good of shareholders and the corporation.

The debate concerning the case for empowering shareholders, which was essentially US-specific, emerged just prior to the global financial crisis, although its roots arguably go back several decades earlier[135].

The shareholder empowerment debate is related to whether US corporate law should make greater use of governance strategies involving appointment and decision rights, to bolster the position of investors vis-à-vis the board of directors.[136]On one side of the debate, Professor Bebchuk strove for an increased use of governance strategies in several key areas of US corporate law, including director elections and amendment of corporate constitutions[137]. In the director election context, Bebchuk proposed 'proxy access' reforms, which were designed to give US shareholders stronger rights in the director nomination process for contested board elections, via access to the corporation's own proxy material. Like shareholder empowerment itself, proxy access was not a new debate in US corporate law – it had laid beneath the surface for at least fifty years. [138] Bebchuk claimed that, without proxy access reforms,

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[135] E.g. William L. Cary, Federalism and Corporate Law: Reflections upon Delaware, 83 YALE
L.J. 663, 666 (1974)

[136] See Jennifer G. Hill, The Rising Tension Between Shareholder and Director Power in the
Common Law World, 18 CORP. GOVERNANCE: AN INT'L REV. 1 (2010) (discussing competing
arguments in the US shareholder empowerment debate).

[137] See Lucian A. Bebchuk, The Case for Shareholder Access to the Ballot, 59 BUS. LAW. 43
(2003) Lucian A. Bebchuk, The Myth of the
Shareholder Franchise, 93 VA. L. REV. 675, 696-7 (2007) ;Lucian A. Bebchuk, 119 HARV. L. REV. 1784 (2006) ;Lucian A. Bebchuk,. 833, (2005) [hereinafter Bebchuk, The Case for Increasing Shareholder Power] (discussing amendment of
the corporate constitution).

[138] Lucian A. Bebchuk & Scott Hirst, Private Ordering and the Proxy Access Debate , 65 BUS .
LAW . 329 (2010); Richard M. Buxbaum, The Internal Division of Powers in Corporate

shareholders' notional power to replace directors in the United States was, in fact, illusory.

Bebchuk's pro-empowerment ideas relied on both efficiency and accountability rationales. It envisaged increased shareholder participation in corporate decision making as an alternative, and less intrusive, governance mechanism, to external intervention by legislators and regulators. The results of years of debate and maybe the influence of important authors such it is Bebchuk have led to a first sign of sea-change in the US corporate law.

The 2006 Paulson Committee Report suggested that an independent justification for stronger shareholder rights was the deep discrepancy in the power imbalance between management and shareholders under US corporate law.[139]

The shareholder empowerment reform agenda faced and still sees strong opposition. Anti-empowerment scholars claimed that, instead of improving US economic competitiveness, reforms granting shareholders stronger legal powers would potentially destroy it. Commentators, such as Professor Stephen Bainbridge, asserted that shareholder lack of power was not a weakness of US corporate law, but rather was a hallmark and a natural corollary of centralized board authority.[140] They sustained that

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Governance ,
73 CAL . L. REV . 1671 (1985); Lewis J. Sundquist III, Comment, Proposal to Allow Shareholder
Nomination of Corporate Directors: Overreaction in Times of Corporate Scandal , 30 WM MITCHELL
L. REV . 1471 (2004). See e.g., Richard M. Buxbaum, The Internal Division of Powers in Corporate
Governance , 73 CAL . L. REV . 1671, 1682-3 (1985) (noting the SEC's 'jawboning' on this issue)

[139] Committee on Capital Markets Regulation, supra note 41 at 103. This approach essentially
ignored the pressures of the market for corporate control. See e.g., Henry Butler Manne, Mergers and
the Market for Corporate Control , 73 J. OF POL . ECON . 110 (1965).

[140] Stephen M. Bainbridge, Director Primacy and Shareholder Disempowerment , 119 HARV . L.

shareholder protection was a more effective regulatory tool than participatory rights, and that shareholders already enjoyed enough protection accorded by the market; the ability to exit and to diversify holdings.

Shareholders were represented as predators or disloyal agents and this negative image were at the basis of many anti-empowerment arguments.

The reasons that were usually brought for restricting shareholder participation in corporate governance were, for example: the risk of balkanized, politicized and dysfunctional boards;[141] board blackmail; abuse of power and opportunistic conduct by sectional shareholder interests; impulsive and reckless conduct by majority shareholders; and a dangerous shareholder preference for short-termism.48 Some commentators were sufficiently alarmed by the specter of stronger shareholder participation rights that they called "for adoption of the 'precautionary principle', commonly used in environmental protection arena", to assess any reforms that might shift the balance of power in shareholders' favor.

An alternative strand of the anti-empowerment argument contended that shareholders themselves did not want stronger participatory rights in corporate governance.

These objections however were not completely heard by the legislator during the presidency of Obama.

Recent US corporate governance developments show that, not only are institutional investors deeply interested in gaining stronger participation rights in corporate

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REV . 1735, 1736 (2006); Martin Lipton & William Savitt, The Many Myths of Lucian Bebchuk , 93 VA .
L. REV . 733, 740; Strine, Towards a True Corporate Republic , 1763; Martin Lipton, Twenty-Five Years After Takeover Bids in the Target's Boardroom: Old Battles, New Attacks and the
Continuing War , 60 BUS . LAW. 1369, 1377 (2005).

[141] Lipton & Savitt, supra note 45 at 748-9; Letter from Henry A. McKinnell, Chairman, Bus.
Roundtable, to Jonathan G. Katz, Sec'y, SEC 4-6 (Dec. 22, 2003) available at https://www.sec.gov/rules/proposed/s71903/s71903-381.pdf .

governance, but that, contrary to the oppositions of some anti-empowerment scholars,[142] they are also prepared to use those rights. Furthermore, institutional investors have become increasingly critical of restrictions on their legal rights effected by the adoption of governance structures, such as dual-class voting rights, which are common in the media and technology sectors.53

3.9 US REFORM ON SHAREHOLDER'S POWERS

One of the aftermaths of the global financial crisis was the need of restoring investor trust providing new policy for stronger shareholder rights and increasing pressure for legislative for a decisive change.

In this new setting, proxy access re-emerged as emblematic of the broader shareholder empowerment debate in the United States.[143] In 2009, the SEC, after not taking any position on the issue for several years, finally decided to introduce a rule implementing proxy access[144].

The Shareholder Bill of Rights put forward numerous governance strategies designed to shift the balance of power within US public corporations in favor of shareholders. These proposals triggered strong opposition and intense political lobbying by corporations.

A bunk of corporate governance changes was introduced under the Dodd-Frank Act of 2010, the future of which is uncertain seen Presidency of Trump.

These reforms, although extremely controversial at the time, were, in fact, far more modest than the Shareholder Bill of Rights proposals, which the Act superseded.

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[142] Bainbridge, 1745, 1751-3; Yair Listokin, If You Give Shareholders Power, Do They Use It? An Empirical Analysis, 166 J. OF INSTITUTIONAL & THEORETICAL ECON . 38 (2010).

[143] See David Skeel Jr., (2016-7) 1-5-8.

[144] Press Release, SEC, SEC Votes to Propose Rule Amendments to Facilitate Rights of Shareholders to Nominate Directors (May 20 2009) available at https://www.sec.gov/news/press/2009/2009-116.htm ; Hill, supra note 33 at 347-9.

Some the most important sea-changing provisions of the Shareholder Bill of Rights, such as those concerning the staggered boards and majority voting, disappeared completely during the legislative reform process. Others were included in the Dodd-Frank Act, but in a lighter form.

One apparently significant corporate governance provision of the Dodd-Frank Act was § 971.[145] This part laid the administrative groundwork for federal right of proxy access, by recognizing the SEC's authority to make rules granting shareholders the right to nominate directors via the company's own proxy materials.[146] Like many other provisions of the Act, § 971 was weaker than the Shareholder Bill of Rights proposals in several ways. First, although § 971 merely authorized the SEC to make proxy access rules, the analogous provision in the Shareholder Bill of Rights required it to make such rules.[147] Secondly, whereas § 971 only provided the SEC with general rule-making authority, the Shareholder Bill of Rights included specific preconditions for proxy access, which were quite concessive with shareholders. § 4 of the Shareholder Bill of Rights, for example, granted proxy access to a shareholder, or group of shareholders, beneficially owning not less than 1% of voting shares for a continuous

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[145] C.f. Marcel Kahan & Edward B. Rock, The Insignificance of Proxy Access, 97 VA. L. REV. 1347 (2011) (discussing proxy access as insignificant on the basis that mutual and pension funds are passive investors and would be unlikely to make use of it).

[146] Delaware had in fact undertaken a 'preemptive strike' in this regard in 2009, when it introduced a new provision, DEL . G.C.L. § 112, which expressly permitted Delaware corporations to adopt bylaws granting shareholders proxy access rights. See Lisa M. Fairfax, Delaware's New Proxy Access: Much Ado About Nothing? 11 TRANSACTIONS: THE TENN . J. OF BUS . L. 87, 104 (2009); On its face, DEL . G.C.L. § 112, in combination with DEL . G.C.L. § 109, appeared to enable shareholders to adopt proxy access bylaws. This was, however, a phantom right only, under since federal law, only the board of directors had the ability to adopt this type of bylaw. See Lisa M. Fairfax, Delaware's New Proxy Access: Much Ado About Nothing? 11 TRANSACTIONS : THE TENN . J. OF BUS . L. 87, 101-3 (2009).

[147] Shareholder Bill of Rights Act of 2009, S. 1074, 111th Cong.
§ 4 ("[t]he Commission shall establish rules relating to the use by shareholders of proxy solicitation materials supplied by the issuer for the purpose of nominating individuals to membership on the board of directors of an issuer" (emphasis added)).

period of at least 2 years before the next scheduled annual meeting.
Following the passage of the Dodd-Frank Act, the SEC adopted Rule 14a-11 under the Securities and Exchange Act of 1934, granting shareholders proxy access in limited circumstances. These circumstances were more restrictive than the preconditions in § 4 of the Shareholder Bill of Rights. Rule 14a-11 adopted a 3%/3 year/25% rule, which granted proxy access to a shareholder, or group of shareholders, holding at least 3% of the company's shares for the previous 3 years, with nominations restricted to 25% of the board of directors.
Analyzing the difference in texts of the Shareholder Bill of Rights and of the Dodd-Fran Act it appears clearly that the § 971 of the Dodd-Frank Act, merely authorized, but did not impose, the SEC to make proxy access rules and the SEC as instead does the Shareholder Bill of Rights.

3.10 RECENT US DEVELOPMENTS

Recent developments in corporate governance' changes passed through the private ordering[148] of shareholders. Notwithstanding the restrictions on shareholders' participatory rights under US corporate law, shareholders in public corporations have gained considerable success with this strategic line.
Private ordering can be used to change the allocation of power between the board of directors and shareholders by using either amendment to the corporate charter or the bylaws. The ability of shareholders to alter the charter is extremely limited in the

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[148] It refers to a long-standing legal concept in which individual parties agree on how to police an activity, instead of relying on government regulation.
To activist investors, it refers to how shareholders agree, with each other and with company management, on how corporate governance will work at a given portfolio company. They do so instead of relying on states, Congress, and the SEC to prescribe corporate governance principles as law and regulation.

The United States. Under Delaware law, only the board of directors can initiate charter amendments.

Albeit the restrictions on the charter amendment under US law, the number of governance-related charter amendments in public corporations incremented sharply during the last decade, with shareholder pressure that represented an important contributing tool.[149]

Bylaws, as explained in the previous paragraphs, can be amended by the shareholders that can exercise their autonomy; this power is limited by the principle that the bylaws cannot be 'inconsistent with law or with the certificate of incorporation'. This generates a catch situation between §§ 109(b) and 141(a) of the Del. G.C.L., which entrust the management power in the board of directors unless otherwise provided by the statute or the charter, and renders the bylaws subservient to the charter in terms of power allocation.

Thanks to this power to amend bylaws and following the SEC's failure to issue mandatory federal rules, institutional investors relied on this private ordering ability to acquire proxy access rights on a company-by-company basis.

Shareholder proposals relating to general corporate governance issues have been in the spotlight in recent years. During the 2015 proxy season, there were 462 such proposals submitted (a 5.5% increase from 2014) and shareholders voted on 333 of those proposals (a 34% increase from 2014). In the 2016 proxy season, there was a decline in the number of corporate governance shareholder proposals submitted (418 proposals) and voted on by shareholders (266 proposals), however, this was partially explained by greater board responsiveness to shareholder demands.

Shareholder proposals during this period focused on an array of corporate governance matters, including board diversity, director qualifications, separation of the roles of chair and CEO,[150] and tenure reforms.

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[149] Geeyong Min, Shareholder Activism and Charter Amendments, UNIV . OF VA. L. SCH. L. & ECON. RES. PAPER, Aug. 15 2016.

[150] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) § 972 requires an issuer to disclose why it has, or has not, decide to split the role of chair and CEO. In December 2016 Wells Fargo & Company announced that its board of directors had amended the bank's bylaws to require separation of these roles. See Press Release, Wells Fargo, Wells Fargo Amends By-Laws to Require

Shareholder proposals relating to proxy access rose from only 17 in 2014, to over 100 at US public corporations in the 2015 proxy season.

Some boards, including those at Bank of America, Citigroup and General Electric (‘GE') voluntarily adopted, or agreed to support shareholder proxy access.

By late 2015, a total of 80 US corporations had adopted proxy access bylaws. By mid-2016, this number had risen to over 240, and included approximately 39% of all approach to these proposals.

At the same time, that proxy access shareholder proposals have expanded, there has been a decrease in the number of proposals concerning to familiar corporate governance issues, such as majority voting, the right of shareholders to convene special meetings and declassification of staggered boards. This decline, however, is itself the prove o shareholders’ overall success in rewriting corporate governance rules through private ordering.

3.11 EU RECENT DEVELOPMENTS

Separation of Chairman and CEO Roles (Dec.1.2016) available at: https://www.wellsfargo.com/about/press/2016/sepa-ration-chairman-ceo-roles_1201/. This announcement came only two days after the State Treasurers of Connecticut and Illinois filed a shareholder resolution calling for a bylaw amendment to this effect. See Press Release, Office of Illinois State Treasurer Michael W. Frerichs, Treasurer Frerichs Signs Resolutions Calling on Wells Fargo to Require Independent Board Chair (Nov. 29 2016) available at: http://illinoistreasurer.gov/TWOCMS/media/doc/November2016TMFWellsFargoResolution.pdf. In general, however, shareholders tend to have had less success in pushing for separation between the chair and CEO than for other types of corporate governance reform such as majority voting and declassification of staggered boards. Also, a number of US companies, such as Walt Disney and Bank of America, have at times split the roles of chair and CEO under pressure from shareholders, only to recombine them several years later. See David F. Larcker & Brian Tayan, Chairman and CEO: The Controversy Over Board Leadership Structure, STAN. CLOSER LOOK SERIES CORP. GOV. RES. INITIATIVE, June 2016, https://www.gsb.stanford.edu/faculty-research/publications/chairman-ceocontroversy-over-board-leadership-structure.

The European Commission has recently pursued modernizing and harmonizing shareholder rights in the European Union (EU) for close to a decade. In particular in its May 2003 Action Plan stated that shareholder engagement at company general meetings was a particular priority, and set out to remove the obstacles that prevented cross-border shareholders mainly from exercising their participation rights (European Commission 2004). The Shareholder Rights Directive 2007/36/EC (the Directive) was finally adopted in July 2007, introducing minimum standards in shareholder admission to meetings, the dissemination of meeting-related information, proxy allocation and distance voting, and participation rights in terms of shareholders asking questions and tabling proposals of their own. This pro-shareholder tendency has been further deepened with the onset of the Global Financial Crisis, with the European Commission (2011) releasing a Green Paper on the European corporate governance framework and the governance role of institutional investors, and member states updating their corporate governance regulations to better accommodate shareholder voice. Empirical research on the role and benefits of shareholder engagement in Europe nonetheless remains limited, largely given to data availability constraints. There is ample evidence that in the US, shareholder activism both at general meetings (e.g. Ertimur et al. 2010; Renneboog and Szilagyi 2011) and behind the scenes (e.g. Bradley et al. 2010; Greenwood and Schor 2009) plays a useful role in addressing managerial agency problems. The European Commission (2006) and Hewitt (2011) only provide descriptive analyses of shareholder participati**on** at European general meetings.The researches carried out by Luc Renneboog of the Tilburg University and by Peter G. Szilagyi of the University of Cambridge on a bunk of 42,170 management proposals and 329 shareholder proposals submitted to general meetings in 17 European countries during the period between 2005 and June 2010, and in particular focusing on investigating the impact of not only meeting, proposal and firm characteristics, but the various regulatory conditions that have been argued to have effect on shareholder participation at general meetings, have lead to the conclusion that the Directive points to the right direction in enabling shareholder engagement. While shareholder dissent at European general meetings still remains limited, there is evidence that it tends to be well-placed. The level of dissent over management proposals is mostly driven by the proposal characteristics, with shareholders predominantly objecting to the adoption of anti-takeover devices and executive compensation. Shareholder proposals are most likely to be submitted to large and poorly performing firms, which indicates that as in the US, the sponsoring shareholders have the "correct" objective of disciplining management. The shareholder proposals targeting anti-takeover devices are by far the most successful, again showing that the voting shareholders seek to discipline management, through exposure to the market for corporate control. Shareholder dissent has increased somewhat over time, with management proposals enjoying less and shareholder proposals receiving more support. However, management proposals still attracted an average 96.3 per cent of the votes cast in 2010, and there is no evidence that the number of shareholder proposals gathered has increased at all, all else equal. This still-limited scope of shareholder participation can partly be explained by the concentrated ownership structures of Continental European firms in particular. The presence of controlling-interest shareholders, as well as deviations from the one share-one vote principle, has generated the so-called "rational apathy" among minority shareholders. The authors of the researchers found that investment funds and other pressure-insensitive institutional investors are prepared to vote against management proposals, and their own proposals enjoy relatively strong support from other shareholders. Nonetheless, they remain – and post-crisis have increasingly been – criticized for not being sufficiently engaged by both regulators and academics (European Commission 2011; McCahery et al. 2010). National regulations play a very pivotal role in galvanizing shareholders, lending strong support to the provisions of the Directive. Dissent against management proposals is significantly greater when shareholders can freely trade their shares and exercise their voting rights, including when there is no share blocking, record date restrictions are reduced, and electronic voting is permitted. Shareholder proposals become more frequent when minimum ownership requirements are reduced, and shareholders are better able to access information and communicate with other shareholders. The voting support for shareholder proposals is also increased by the abolishment of share blocking. Moreover shareholders tend use their votes to address governance concerns at the firm-level when concerned about the general governance and institutional environment. Giving the chance to shareholders to raise their voice at general meetings is a part of good governance, and the shareholders themselves are discerning enough that they will not do so unless deemed necessary. Luc Renneboog and Peter G. Szilagyi conclude that not only is the Shareholder Rights Directive a move in the right direction, national regulators should go beyond the minimum standards introduced by the Directive in order to increase the support shareholder rights.

3.12 THE ROLE OF SHAREHOLDER ENGAGEMENT IN CORPORATE GOVERNANCE

Shareholder interventions in corporate governance can be placed on a continuum of responses that shareholders can give to concerns over managerial performance and governance quality. At one extreme, shareholders can simply vote with their feet by selling their shares. At the other extreme is the market for corporate control, where investors initiate takeovers and buyouts to bring about fundamental corporate changes (Gillan and Starks 2007). The role of shareholder interventions as a disciplinary mechanism has historically been widely debated. Bebchuk (2005) argues that it has an important role in mitigating the agency problems associated with managerial decisions. Harris and Raviv's (2010) theoretical paper agrees, by showing that when agency concerns are exacerbated in the firm, it is always optimal that shareholders seek control over corporate decisions. Opposing arguments nonetheless remain, especially in the legal literature. Lipton (2002) and Stout (2007) argue that shareholders can be beset with conflict of interest motivations, or be simply too uninformed to take effective governance decisions. Bainbridge (2006) goes as far as claiming that activist shareholders can outright damage the firm by disrupting the authority of the board of directors, and infers that shareholder voice should actually be restricted. Albeit these concerns, regulators have actively promoted shareholder engagement at company general meetings since the onset of the Global Financial Crisis. Indeed, Masouros (2010) argues that there is a clear pro-shareholder tendency around the world, despite marked differences in national corporate governance regimes. The United States (US) led the charge with the adoption of the Dodd-Frank Wall Street Reform and Consumer Protection Act in July 2010, and the subsequent measures taken by the Securities and Exchange Commission (SEC) to (i) introduce say-on-pay and say-on-golden parachutes provisions, (ii) permit shareholder proposals on CEO succession, and (iii) allow certain shareholders proxy access for director nominations, subject to majority consent. In the EU, a pro-shareholders Directive was adopted in 2007 so it actually predates the crisis, but it also promotes shareholder voice at general meetings. Many European countries have since updated their corporate governance codes not only to transpose the Directive but to implement further reforms always in the light of a major shareholder engagement. The recent US literature implies that efforts to promote shareholder engagement at company general meetings point to the right direction. Ertimur et al. (2010) and Renneboog and Szilagyi (2011) show that shareholder proposals submitted to meetings tend to target firms that underperform and have poor governance structures. The authors find no evidence of systematic agenda-seeking by activists, as well as show that the voting shareholders tend to only support proposals with discernible control benefits. They also argue that the control benefits of shareholder interventions are at least partly realized from the reputational pressure imposed on management, rather than the interventions themselves. Indeed, Buchanan et al. (2012) find that firms targeted by shareholder proposals are subsequently more inclined to replace their CEOs and elect independent board chairmen. Each of these studies show that shareholder interventions with clear control benefits are met with positive market reactions. The empirical evidence on the benefits of behind-the-scenes interventions circumventing general meetings is decidedly more mixed. In the US, pension funds shifted towards private negotiations with management in the early 1990s, although their interventions are relatively non-controversial despite some concerns (Woidtke 2002). Private engagement by hedge funds and other investment funds has been a much more contentious issue. Hedge funds are well-known to rely on controversial activist strategies, whereby they take positions in underperforming firms and target management directly. A point of concern has been that these interventions may push towards short rather than long-term gains, resulting in investment inefficiencies and excessive leverage (Becht et al. 2009; Bradley et al. 2010; Brav et al. 2008; Clifford 2008; Greenwood and Schor 2009; Klein and Zur 2009). Empirical research on the role and benefits of shareholder engagement in Europe remains relatively rare. Buchanan et al. (2012) compare shareholder proposals submitted to general meetings in the US and the UK, and find that while there are systematic differences in the proposal objectives, the sponsor identities as well as the voting outcomes, the target firms tend to be poorly performing in both countries. This is confirmed by Cziraki et al. (2011), who examine shareholder proposals submitted in both the UK and Continental Europe. The authors also emphasize, however, that shareholder interventions at European company meetings are not met with positive market reactions and remain relatively rare. Girard (2009) studies activist strategies in France, and reports that civil lawsuits are the preferred tools of activists engaging firms over governance concerns, and that this particularly aggressive strategy is also the most likely to succeed. Becht et al. (2009) examine the strategies of a single UK investor, the Hermes UK Focus Fund, and confirms that the fund predominantly pursues behind-the-scenes negotiations with management. The authors attribute the success of this strategy to the credible threat that if management refuses to negotiate, the fund will call an extraordinary meeting, with the looming prospect of a proxy fight. The credibility of this threat is underpinned by the fact that unlike in the US, proposals that pass the shareholder vote are legally binding in the UK, as in most of Europe, and shareholders can remove directors by an ordinary proposal.

3.13 PARTICIPATION AT EUROPEAN GENERAL MEETINGS

General meetings are the formal forum where firms present relevant matters to shareholders, and where shareholders vote upon these matters and put questions to management. However, shareholder absenteeism remains significant in much of Europe. In the market-oriented corporate governance regime of the UK, the average turnout rate is 68 per cent on average (Hewitt 2011), while the turnout of companies' free float – shares not held by managers, directors or controlling shareholders – is 40-52 per cent (European Commission 2006). In the stakeholder-oriented governance regimes of Continental Europe, shareholders are far less engaged. Turnout rates are less than 60 per cent on average and below 50 per cent in Belgium, Denmark, Norway and Switzerland. The gap is even more pronounced in the turnout of companies' free float, which stands at only 17 per cent in France, 10 in Germany and 4 in Italy. The obstacles that limit shareholder engagement at European company meetings have long been part of the dialogue on the future of European corporate governance. Zetzsche (2008) argues that low turnout rates in Continental Europe are partly due to concentrated ownership structures, which have historically remained in place due to poor shareholder protection (La Porta et al. 1998; Martynova and Renneboog 2008). Dominant shareholders are obviously strongly motivated to participate and vote at meetings, which should technically boost turnout levels. However, their presence exacerbates "rational apathy" among minority investors, i.e. the perception that their vote would make little difference. Indeed, while US firms tend to have widely dispersed ownership structures, their average turnout rate is 82 per cent. Ownership is slightly more concentrated in the UK and significantly more concentrated in Continental Europe. Of UK listed firms, 63 per cent are regarded as being widely held, and the typical voting block is twice the size of that in the US, at around ten per cent. In contrast, the largest voting blocks often constitute controlling interest in Continental Europe, reaching 20 per cent on average in France, 44 in the Netherlands, and 57 in Germany (Becht and Mayer 2001; Faccio and Lang 2002; Goergen and Renneboog 2001). The types of blockholders present are also quite different. Blockholders in the US and the UK tend to be corporate insiders and institutional investors (Becht 2001). In contrast, 50-60 per cent of Continental European firms are effectively owned by families, and many are controlled by banks that both sit on the board and extend their voting power by voting the shares deposited with them (Barca and Becht 2001; Faccio and Lang 2002; Franks and Mayer 2001; La Porta et al. 1999; Nibler 1998). The more immediate concern of European regulators is that due to a variety of reasons, minority shareholders in Continental Europe must bear significant costs to exercise their participation rights, without enjoying the economies of scale that concentrated owners do. These costs include not only procedural but information and decision-making costs. The European Commission (2006), the OECD (2007) and Georgeson (2008) report that the main impediments to shareholder engagement in Europe have been (i) limited access to information about upcoming and past meetings; (ii) limited access to meetings e.g. through share blocking, which requires participating shareholders to deposit their shares; (iii) restrictions on proxy allocation and distance voting; and (iv) restrictions on shareholder engagement, including the right to ask questions, call general meetings, and submit shareholder proposals. Cross-border investors find the procedural and information costs of meeting participation particularly burdensome. Cross-border investment has been actively push by the EU to create integrated financial markets, and has now reached over 40 per cent of market capitalization on average (FESE 2008). However, foreign attendance at general meetings still suffer of poor numbers. Foreign investors typically hold their shares through accounts with securities intermediaries, which in turn hold accounts with other intermediaries and central securities depositories. To vote in absentia, they must go through global custodian banks, or their proxy vendors, which in turn must engage proxy-related services from local market subcustodians (OECD 2011). The European Commission (2006) argues that overall, the administrative costs of cross-border voting are twice the costs of domestic voting, and are largely prohibitive for foreign investors.

3.14 THE SHAREHOLDER RIGHTS DIRECTIVE

The impediments to shareholder participation at general meetings were widely acknowledged during the public consultation launched by the European Commission in 2004, and subsequently formed the motivation behind the adoption of the Shareholder Rights Directive (Directive 2007/36/EC) in July 2007. The Directive expressly states that effective shareholder control is a prerequisite to sound corporate governance and should, therefore, be facilitated. Its declared aim is "to strengthen shareholders' rights, in particular through the extension of the rules on transparency, proxy voting rights, the chance of participating in general meetings via electronic means and ensuring that cross-border voting rights are able to be exercised". The key provisions of the Directive include:

a minimum notice period of 21 days; this can be reduced, if shareholders agree in a public vote, to 14 days if electronic voting is permitted;

- internet publication of the convocation and any documents submitted to the GM at least 21 days before the GM;
- abolition of share blocking, and introduction of a record date that may not be more than 30 days before the GM;
- abolition of obstacles to voting by post and electronic voting;
- right to ask questions and obligation on the part of management to answer questions;
- abolition of constraints on eligibility to act as proxy holder and of excessive requirements for the process of proxy appointment;
- the possibility that shareholders put items on the agenda and table draft resolutions for items on the agenda, with a minimum ownership requirement that does not exceed five per cent of the company's share capital;
- disclosure of voting results on the firms's interests website;

While the Directive has generally been regarded as a move in the right direction, it is still criticized for imposing only minimal standards that still fail to ensure a level playing field for all shareholders. For instance, Davies et al. (2011) argue that cross-border shareholders often remain uninformed about future meetings, and their votes are often not exercised, or exercised by others, due to the intermediaries they go through. Masouros (2010) adds that the provision on shareholder proposals is "empty letter", because the five per cent ownership threshold is still highly prohibitive, and shareholders are unable to communicate and form coalitions due to a lack of infrastructure for proxy solicitation and even access to share registries. Many countries have showed a reluctance in the transposition of the Directive itself by not implementing the content of it in their national legal systems.

3.15 SHAREHOLDER ACTIVISM AT EUROPEAN GENERAL MEETINGS

Shareholders in the US are not entitled to call extraordinary meetings unless the corporate charter or bylaws allow otherwise. However, each year between 1996 and 2005, an average 14.1 per cent of S&P 1500 firms were targeted by shareholder proposals, peaking at 21.3 per cent in 2003 (Renneboog and Szilagyi 2011). This largely owes to SEC's fairly liberal Rule 14a-8 governing shareholder proposals, which allows submissions to be made by any shareholder owning USD2,000 or one per cent of voting shares. While there is now ample evidence that shareholder proposals play a useful and relevant role in US corporate governance (Buchanan et al. 2012; Ertimur et al. 2010; Renneboog and Szilagyi 2011), the Directive stop short of truly encouraging proposal submissions in Europe. The five per cent minimum ownership requirement is indeed quite stringent and, had already been met by all EU member states. This very cautious approach may be due to ongoing concerns that shareholder activism can come at a cost. European policymakers also often argue that US lessons on the governance role of shareholder proposals may not be readily applicable in the European context. Firstly, proposals in the US are non-binding even if they pass the shareholder vote, whereas they are legally binding in Europe.Secondly, cross-country differences in the regulation of proxy solicitation may affect the incentives of and costs borne by activist shareholders. And thirdly, the market-oriented Anglo-American governance model is indeed quite different from the stakeholder-oriented regimes of Continental Europe. It is important to keep in mind that in Continental Europe, the investor base that is likely to submit and lend voting support to shareholder proposals is relatively narrow. Foreign shareholders tend to be institutional investors, but they often face prohibitive high voting costs. Of domestic institutions, pension funds, insurance firms and investment funds hold 41 per cent of equities in the UK, but only 29 in France, 14 in Germany and Italy, and 8 in Spain (FESE 2008). Many of these investors also pursue predominantly passive investment strategies, preferring to vote with their feet by selling their shares. McCahery et al. (2010) find that 80 per cent of institutional investors would consider selling rather than engaging, and while 66 would vote against management to address governance concerns, only ten would expose their concerns publicly. Indeed, institutional investors have often been criticized in particular in the post-crisis, for their passivity and not doing enough due diligence.

3.16 CONCLUSION AND POLICY IMPLICATIONS

There is now considerable evidence in the US academic literature that shareholders participating at company general meetings are valuable monitoring agents. In Europe, the empirical investigation of this issue has been complicated by data availability, as well as the fact that European countries are very diverse in terms of ownership structures, legal provisions governing shareholder rights, as well as the monitoring incentives of and costs suffered by shareholders. Shareholder absenteeism still is frequent in Continental Europe in particular due to "rational apathy", and voting dissent at general meetings has increased only marginally in the last decade.

Whether shareholder participation in corporate governance should be facilitated has been subject to heated policy debate around the world. With the onset of the Global Financial Crisis a clear pro-shareholder tendency emerged, and corporate governance rules have been updated accordingly due to the new-coming need. Nonetheless, regulators continue to drag their feet about truly enabling shareholder voice. The European analysis presented in this has confirmed that shareholder engagement at general meetings is actually a part of good governance and for this reason it should be perceived. Shareholders tend not to have self-serving agendas and are discerning enough to only intervene at the "correct" firms and when deemed necessary. In fact, there is evidence that they use their voice not simply to discipline underperforming managers, but also to make up for inefficiencies in the broader governance and institutional environment that potentially would bring to managerial agency problems and underperformance in the first place. Ultimately, national regulators in the European Union should go beyond the minimum standards introduced by the Shareholder Rights Directive to support shareholder participation in corporate governance. The Directive's provisions still fail to ensure a level playing field for all shareholders. The procedural and information costs of cross-border voting remain largely prohibitive and must be further reduced. Communication between atomistic minority shareholders should be enabled, including by promoting registered rather than bearer shares while easing registration rules, and by reducing and harmonizing ownership disclosure thresholds. Shareholders should also have access to company proxies and face less stringent minimum ownership requirements to introduce their own proposals. Some proposals may even be made routinely put to shareholder vote to reduce the need for shareholder intervention, as has been the case for some form of say-on-pay not only in the US and the UK, but in Belgium, Denmark, Italy, the Netherlands and Sweden, among others. As a conclusion the rules governing shareholder engagement at European general meetings should be further relaxed and harmonized. Minority shareholders are useful monitoring agents, and it is clear that criticism that they might abuse their rights is exaggerated. It is critical to point out that beyond helping to address the managerial agency concerns highlighted by the Global Financial Crisis, the harmonization of shareholder voice would also aid the European Commission's declared objective of deepening equity market integration within the EU. The fundamental purpose of integration is to create liquid markets that bring down financing costs for European firms. However, shares will always trade at a discount if investors cannot freely exercise the voting rights attached to them. Market liquidity will also continue to be hindered by the persistence of concentrated ownership structures, which have historically remained in place in countries where shareholders have been hesitant to diversify due to restrictions on the rights of minority shareholders.

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