

Legal Framework for Promoting Minority Shareholders' Protection in Thailand

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Abstract

Since the Asian currency crisis the legal framework for protecting minority shareholders in Thai listed companies has been strengthened. International and Western legal principles have been adopted to improve its efficiency and effectiveness. The main purpose has been to grow investment. The research questions whether the adopted legal principles are appropriate in the Thai context. It considers: (i) whether the existing Thai legal framework provides adequate protection for minority shareholders; (ii) whether the transplanting of legal frameworks from other jurisdictions into Thai law is feasible; and (iii) what the obstacles to legal reforms are.

The background to relevant aspects of the Thai economic, legal and regulatory systems relating to listed companies is described, as well as the relationship between growth in investment in shares and shareholders' protection. Related Thai legislation, case law, regulatory policies and secondary literature are analysed. Key developments in German, United States and Delaware law are considered. The Thai legal system is based on German law which in turn has been significantly influenced by Roman Law. United States law has increasingly shaped principles adopted in international law and the law of developing jurisdictions, including Thailand. The research incorporates the analysis of interviews undertaken in 2010 on the regulation of Thai listed companies and the implementation of transplanted principle, with 21 participants. The data obtained from the literature and interviews is used to create an understanding of Thai law and regulatory practices and to suggest further legal reform.

The findings confirm that Thai law on minority shareholders' protection is significantly influenced by United States and Delaware law. The existing law provides adequate protection for minority shareholders but some of the adopted laws are not able to function. This is due to the difference between the contexts of the borrowed and the receiving jurisdictions. The research suggests that more attention be given to re-examining the adopted rules, educating legal agents, and strengthening legal enforcement.

Declaration

I, Nilubol Lertnuwat, declare that the PhD thesis entitled Legal Framework for Promoting Minority Shareholders' Protection in Thailand is no more than 100,000 words in length including quotes and exclusive of tables, figures, appendices, bibliography, references and footnotes. This thesis contains no material that has been submitted previously, in whole or in part, for the award of any other academic degree or diploma. Except where otherwise indicated, this thesis is my own work.

Signature

Date

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List of Publications

Nilubol Lertnuwat, 'Legal Framework for Promoting Minority Shareholders' Protection in Thailand: Lessons from Australian Experiences' (Paper presented at Academic Seminar for Legal Education Development Project organised by Commission on Higher Education and Office of Justice Affairs, Bangkok, Thailand, 30 April 2008).

N Lertnuwat, 'The duties of directors and controlling shareholders in Thai listed companies' (2011) 26 *Aust Jnl of Corp Law* 165.

Table of Contents

Title	i
Abstract	ii
Declaration	iii
Acknowledgements	iv
List of Publications	v
Table of Contents	vi
List of Figures	xii
List of Tables	xiii
List of Selected Abbreviations	xiv
Table of Cases	xv
Table of Statutes	xvii
Chapter 1 Introduction.	1
1.1 Background of the research	1
1.2 Core research questions	8
1.2.1 Does the Thai legal framework provide adequate protection for minority shareholders?	8
1.2.2 Is the transplantation of the legal frameworks applied in other jurisdictions into Thailand feasible?	11
1.2.3 What are the obstacles to legal reform in Thailand?	14
1.3 Research methodology	16
1.3.1 Research design	16
1.3.2 Preparation of the interviews	20
1.3.3 Conduct of the interviews	23
1.3.4 Application of the research material	25
1.3.5 Limitations of the research methodology	27
1.4 Outline of the thesis	28

Chapter 2	The Nature of Minority Shareholders' Protection.	30
2.1	Introduction	30
2.2	Conceptualising minority shareholders	30
2.2.1	The concept of "control"	31
2.2.2	Controlling and minority shareholders	33
2.3	The development of minority shareholders' protection in the United States	35
2.3.1	Agency problems	35
2.3.2	Controlling agency problems	37
2.3.3	Regulatory mechanisms	43
2.4	Minority shareholders' protection under the German model	46
2.4.1	The two-tier board system	47
2.4.2	Co-determination	50
2.4.3	The role of German banks	53
2.5	The concept of minority shareholders' protection in the East Asian context	56
2.5.1	Ownership structure of East Asian corporations	57
2.5.2	The effect of the concentrated-ownership structure	61
2.5.3	The application of the Western corporate governance models	65
2.5	Conclusion	69
Chapter 3	The Legal Framework of Minority Shareholders' Protection in Thailand.	71
3.1	Introduction	71
3.2	Background	72
3.2.1	Thai companies and company law	72
3.2.2	Legal transplants in Thai company law	76
3.2.2.1	The critique on legal transplants	76
3.2.2.2	Four phases of legal transplants in Thai company law	81
3.2.3	The Stock Exchange of Thailand	86

	3.2.3.1 The development of the Stock Exchange of Thailand	86
	3.2.3.2 Individual shareholders' role in the Thai capital market	89
3.3	Reforms to minority shareholders' protection in Thailand	93
	3.3.1 The demand for legal reform in Thailand	93
	3.3.1.1 Government-led policies	94
	3.3.1.2 Demand from the private sector	97
	3.3.2 Post-1997 crisis reform	101
	3.3.2.1 Institutions	102
	3.3.2.2 Code of Corporate Governance	104
3.4	Thai corporate and securities laws on protecting minority shareholders	105
	3.4.1 Corporate law	106
	3.4.2 Securities law	107
	3.4.3 Regulations of the Securities and Exchange Commission .	109
	3.4.4 Regulations and listing rules of the Stock Exchange of Thailand	109
3.5	Securities regulator and law enforcement agencies	110
	3.5.1 The Securities and Exchange Commission	110
	3.5.1.1 Criticisms of the Securities and Exchange Commission	112
	3.5.2 Thai legal enforcement agencies	115
3.6	Conclusion	120
Chapter 4	The Fundamental Rights of Minority Shareholders.	122
	4.1 Introduction	122
	4.2 Shareholders' management rights	123
	4.2.1 Shareholders' participation in shareholders' meetings	123
	4.2.1.1 The right to obtain information on the agendas to be voted	124
	4.2.1.2 The right to vote <i>in absentia</i>	125

	4.2.1.3 The right to propose an agenda	131
	4.2.2 Shareholders' participation in the appointment of board members	135
	4.2.2.1 Cumulative voting	135
	4.2.2.2 Nomination process	137
	4.2.2.3 Independent directors	139
4.3	Proprietary rights of shareholders	144
4.3.1	Maintaining the shareholding	144
4.3.2	Rights to dividends	146
4.4	Conclusion	148
Chapter 5	Duties of Directors and Controlling Shareholders.	150
5.1	Introduction	150
5.2	Duties of directors	150
5.2.1	The general concept of directors' duties	150
5.2.2	The duty of care	153
	5.2.2.1 Business judgment rule	160
5.2.3	Duty of loyalty	166
5.2.4	Avoidance of liability	174
5.3	Fiduciary duties of controlling shareholders	178
5.4	Conclusion	186
Chapter 6	Minority Shareholders' Protection in Specific Contexts.	188
6.1	Introduction	188
6.2	Changes in control	188
6.2.1	Mergers	189
	6.2.1.1 Mergers made by agreement	189
	6.2.1.2 Asset acquisitions	193
6.2.2	Hostile takeovers	196
	6.2.2.1 Proxy contests	197
	6.2.2.2 Hostile bids	199
6.2.3	Freezeouts	210

6.3	Related-party transactions	214
6.4	Conclusion	219
Chapter 7	Minority Shareholders' Remedies.	220
7.1	Introduction	220
7.2	Shareholders litigations	221
7.2.1	Derivative actions	221
7.2.1.1	Introduction	221
7.2.1.2	Provisions on derivative actions	223
7.2.2	Class actions	236
7.3	The securities regulators	240
7.3.1	The roles of securities regulators	241
7.3.2	The roles of securities regulators: compared	251
7.3.3	The power of the Thai SEC: reconsidered	255
7.4	Conclusion	262
Chapter 8	Transplanting Corporate Law: Thailand's Experience.	263
8.1	Introduction	263
8.2	The possibilities of legal transplants: the experience from Thai company law	263
8.3	The success of legal transplants	266
8.4	Where to from here?	271
8.4.1	Adopting the German dual board model	271
8.4.2	Maintaining common law transplantation	276
8.4.3	Strengthening Thai corporate law and regulation	278
8.4.3.1	Family-owned companies	279
8.4.3.2	Independent directors	282
8.4	Conclusion	286
Chapter 9	Conclusion.	287
9.1	Introduction	287
9.2	The background to the research	288

9.3	Conclusions to the research questions	290
9.3.1	Does the Thai legal framework provide adequate protection for minority shareholders?	290
9.3.2	Is the transplantation of the legal frameworks applied in other jurisdictions into Thailand feasible?	293
9.3.3	What are the obstacles to legal reform in Thailand?	296
9.4	Implications and research contribution	300
9.4.1	Implications	300
9.4.2	Research contribution	303
9.4.2.1	Academic contribution	303
9.4.2.2	Practical contribution	305
9.5	Limitations of the study	307
9.6	Suggestions for future research	308
	Appendices	310
	Appendix A: The interview schedule	310
	Appendix B: Information to Participants Involved in Research	314
	Appendix C: Consent Form for Participants Involved in Research	316
	Bibliography	317

List of Figures

3.1	Holding of equity and market turnover compared (2002)	92
5.1	Directors' duty of loyalty under Thai law	172
7.1	Securities regulation costs per billion dollars of stock market capitalisation (2003–2004)	252
7.2	SEC enforcement activity as a percentage of the SEC's total budget (2004–2006)	253
7.3	Amount spent on enforcement by BaFin (2005–2007)	254
7.4	Legal systems' matrix	260

List of Tables

2.1	Characters of the US, German and East Asian corporations	66
3.1	Domestic market capitalisation of Asian Pacific stock markets (2008– 2011)	88
3.2	Number of shareholders by shareholder types	89
3.3	Holding of equity (2002)	91
3.4	Changes in controlling shareholders of Thai listed companies after the 1997 financial crisis	97
3.5	Controlling shareholders of large Thai listed companies in 1996 and 2000	98
7.1	Powers of the securities regulators in the three jurisdictions	251
7.2	Guilty pleas and trials in selected white collar categories	259

List of Selected Abbreviations

BaFin	Bundesanstalt für Finanzdienstleistungsaufsicht [Federal Financial Supervisory Authority]
BAWe	Bundesaufsichtsamt für den Wertpapierhandel [Federal Securities Supervisory Office]
BEX	Bond Electronic Exchange
CEO	Chief executive officer
DGCL	Delaware General Corporation Law
ESAs	European Supervisory Authorities
ESMA	European Securities and Markets Authority
EU	European Union
ROSC	Reports on the Observance of Standards and Codes
DAX	Deutsche Aktienindex [German Stock Market]
DSI	Department of Special Investigation
ECOTEC	Economic and Cyber-Crime Division
GDP	Gross domestic product
GFCF	Gross Fixed Capital Formation
IMF	International Monetary Fund
MAI	Market for Alternative Investment
NYSE	New York Stock Exchange
OECD	Organisation for Economic Co-operation and Development
SEC	Stock and Exchange Commission
SET	Stock Exchange of Thailand
TFEX	Thailand Futures Exchange Plc
Thai SEC	Thai Stock and Exchange Commission
TRIS	Thailand Ratings and Information Systems
US	United States of America

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Securities Enforcement Remedies and Penny Stock Reform Act of 1990

Germany

Aktiengesetz of 2009 [Stock Corporation Act]

Allgemeines Deutsches Handelsgesetzbuch [Commercial Code]

Betriebsverfassungsgesetz of 1952 [Works Constitution Act]

Bürgerliches Gesetzbuch [Civil Code]

Gesetz über die integrierte Finanzaufsicht of 2002 [Financial Services and Integration Act]

Gesetz zur Unternehmensintegrität und Modernisierung des Aktiengesetzes of 2005
[Law on Corporate's Integrity and on the Modernization of the Stock Corporations Act]

Kapitalanleger-Musterverfahrensgesetz of 2005 [Capital Market Model Case Act]

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Stock Exchange of Thailand Notifications

Stock Exchange of Thailand Regulations

Chapter 1

Introduction

- 1.1 Background of the research
- 1.2 Core research questions
 - 1.2.1 Does the Thai legal framework provide adequate protection for minority shareholders?
 - 1.2.2 Is the transplantation of the legal frameworks applied in other jurisdictions into Thailand feasible?
 - 1.2.3 What are the obstacles to legal reform in Thailand?
- 1.3 Research methodology
 - 1.3.1 Research design
 - 1.3.2 Preparation of the interviews
 - 1.3.3 Conduct of the interviews
 - 1.3.4 Application of the research material
 - 1.3.5 Limitations of the research methodology
- 1.4 Outline of the thesis

1.1 Background of the research

In Thailand, as in other Asian countries, concern with minority shareholders' protection increased after the 1997 Asian financial crisis. The crisis firstly impacted Thailand and then spread across Asian economies and finally the global economy.¹ It is claimed that the causes of the 1997 crisis include over-capacity, poor quality of investments, excessive diversification by large companies, excessive exposure to short-term foreign debt, and, most importantly, weakness in corporate governance.² The crisis left small investors seriously damaged by losing their life savings while controlling shareholders

¹ For detailed research on the history of the financial economic crisis in Thailand, see Ammar Siamwalla, 'Anatomy of the Thai Economic Crisis' in Peter Warr (ed), *Thailand Beyond the Crisis* (2005); Peter Warr, 'Boom, Bust, and Beyond' in Peter Warr (ed), *Thailand Beyond the Crisis* (2005); Ek Setthasat, 'Ten Years after the Financial Crisis: The Unforgettable Lesson', *Bangkok Business* (Bangkok), 12 June 2007 <<http://www.nidambe11.net/ekonomiz/2007q3/2007june12p1.htm>> at 20 March 2012.

² Pedro Alba, Stijn Claessens and Simeon Djankov, 'Thailand's Corporate Financing and Governance Structure' (Policy Research Working Paper No 2003, World Bank, 1998) 2–3; Laurent L Jacque, 'The Asian Financial Crisis: Lessons from Thailand' (1999) 23(1) *The Fletcher Forum of World Affairs* 87, 89–91; Juzhong Zhuang et al, *Corporate Governance and Finance in East Asia: A Study of Indonesia, Republic of Korea, Malaysia, Philippines, and Thailand: Volume One (A Consolidated Report)* (2000) 1.

were largely unharmed.³ The severe consequences of the crisis forced Asian countries' attention to the improvement of corporate governance and the protection of small investors in the capital markets.

In addition to the 1997 Asian financial meltdown, other financial crises and corporate failures around the world exposed the need for corporate governance reform. In the United States, for instance, a series of corporate failures from the dot.com crisis in the late 1990s to the collapse of Enron in 2001 increased awareness of the importance of corporate governance and regulation.⁴ To resolve the systemic and structural weakness of the US system, the legislature responded by enacting the Sarbanes-Oxley Act in July 2002. More recently the current global financial crisis reflected the failure of governance, risk management, and regulation in financial corporations in the US and Western Europe. This crisis has also led to reconsideration of the effectiveness of regulating corporate activities and markets.⁵ Corporate governance is being readdressed to regain investors' confidence and reduce the risk of the re-occurrence of corporate failures.⁶ The call for changes in the financial regulatory system has led the US Congress to enact further extensive legislation, including the Wall Street Reform and Consumer Protection Act of 2009, and Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Germany, similarly to the US, was directly hit after the dot.com failure in 2001. During this period, the German stock index dropped 70 per cent from its highest point in 2000.⁷ A striking example is Intershop Communication, a global pioneer of an e-commerce software company. Its stock was valued at the end of 2001 at

³ See, eg, Sea-Jin Chang, *Financial Crisis and Transformation of Korean Business Groups: The Rise and Fall of Chaebols* (2003) 211–2; William Goetzmann and Elisabeth Köll, 'The History of Corporate Ownership in China: State Patronage, Company Legislation, and the Issue of Control' in Randall K Morck (ed), *History of Corporate Governance Around the World: Family Business Groups to Professional Managers* (2005) 182.

⁴ John C Coffee Jr, 'Understanding Enron: "It's About the Gatekeepers, Stupid"' (2002) 57 *Business Lawyer* 1403; Scott Harshbarger and Goutam U Jois, 'Looking Back and Looking Forward: Sarbanes-Oxley and the Future of Corporate Governance' (2007) 40 *Akron Law Review* 1, 2–4.

⁵ International Monetary Fund, *IMF Urges Rethink of How to Manage Global Systemic Risk* (2009) International Monetary Fund, <<http://www.imf.org/external/pubs/ft/survey/so/2009/pol030609a.htm>> at 20 March 2012.

⁶ Grant Kirkpatrick, *The Corporate Governance Lessons from the Financial Crisis* (2009) 2; *Financial Regulatory Reform* (2011) The New York Times <http://topics.nytimes.com/topics/reference/timestopics/subjects/c/credit_crisis/financial_regulatory_reform/index.html> at 20 March 2012.

⁷ *Dotcom Crash: The Worst is over in Germany* (2003) Deutsche Bank Research <http://www.dbresearch.com/PROD/DBR_INTERNET_EN-PROD/PROD0000000000063655.pdf> at 20 March 2012, 3.

approximately €10,000 but at the end of 2005 it had dropped to €27.⁸ The failures also drove the reforms in German company law to better protect minority shareholders.⁹ While the global financial crisis had adversely affected the financial sector of the German economy, it has had a less damaging effect on its real estate sector. Unlike the US and other European countries, real estate prices in Germany had remained low. After the dot.com burst in 2001, Germans were reluctant to invest in real property. Foreign investors were also less active in Germany.¹⁰

The concept of corporate governance is not new but, due to the recent financial crises, it has become prominent in contemporary business, accounting, and legal debates. Corporate governance is frequently defined in the literature but there is no universally agreed definition.¹¹ Despite such dissension over what it is, many scholars affirm its significance. Adam Smith observed in the 1700s that the managers of companies were not as motivated as the shareholders were to protect the shareholders' capital.¹² Rule and procedures to protect shareholders' interests were necessary. Berle and Means in the early 1930s similarly pointed out that the listed US corporations was run by professional managers¹³ and dispersed shareholders no longer had control of the corporation or the managers.¹⁴ Jensen and Meckling further explained the conflicting interests of shareholders and managers in terms of agency theory.¹⁵ To control the problems that agents will never act as efficiently as principals will in protecting the principals' interests, different mechanisms must be used to monitor the managers' actions.¹⁶ This is to ensure the effective and efficient management to achieve the objectives of the firm and its shareholders.

⁸ Guido Buenstorf and Dirk Fornahl, 'B2C – Bubble to Cluster: The Dot.com Boom, Spin-off Entrepreneurship, and Regional Industry Evolution' (Max Planck Institute of Economics Evolutionary Economics Group, 2006) 3.

⁹ Such as the concepts of derivative actions and class actions.

¹⁰ Mark Waffel, *Why the Global Housing Market Boom Bypassed Germany* (2008) Spiegel Online <<http://www.spiegel.de/international/business/0,1518,552901,00.html>> at 20 March 2012

¹¹ James McConvill, *An Introduction to CLERP 9* (2004) 1.

¹² Adam Smith, *Wealth of Nations* (1776) 700.

¹³ See Adolf A Berle Jr and Gardiner C Means, *The Modern Corporation and Private Property* (1933) 3.

¹⁴ Ibid 117.

¹⁵ Michael Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 *Journal of Financial Economics* 305, 308.

¹⁶ The detailed discussion on this issue is in Chapter 2.

Debates on corporate governance are concerned with accountability.¹⁷ In carrying out their functions, directors and senior managers are expected to be accountable for their actions. They are required to explain or justify their decisions.¹⁸ In addition to placing responsibility on management, accountability mechanisms empower shareholders and other stakeholders to monitor and evaluate whether their interests have been well protected. To assist the shareholders and stakeholders in this monitoring, the management is required to disclose material information. The information given must be timely and accurate.¹⁹

The scope of corporate governance is no longer limited in debates over it to management and shareholders. The growing scale of corporations means that decision making within them does not only affect the management and shareholders but also other related people including creditors and employees. The concept of corporate governance has been specifically extended by some writers and interest groups to ethical and moral issues.²⁰ Increasingly literature questions, for instance, whether corporations pay sufficient attention to impacts on the environment or the conditions of their workers. In most models corporate governance is a set of relationships between a company's board of directors, its management, shareholders and other stakeholders.²¹ It distributes rights and responsibilities among different participants both inside and outside the company.²²

Since the financial crisis in 1997, Thailand has been strengthening its law and regulatory practices on minority shareholders' protection.²³ As discussed in detail in

¹⁷ See Margaret M Blair and Lynn A Stout, 'Director Accountability and the Mediating Role of the Corporate Board' (2001) 76 *Washington University Law Quarterly* 403; Larry E Ribstein, 'Accountability and Responsibility in Corporate Governance' (2006) 81 *Notre Dame Law Review* 1476.

¹⁸ William Rees, *Corporate Governance* (1995) 3.

¹⁹ *Ibid* 4.

²⁰ See Peter A Appel and Rick Irvin, 'Public Regulatory Encouragement to the Adoption of Private Ordering Systems to Achieve Environmental Protection through Sustainable Commerce' in PM Vasudev and Susan Watson (eds), *Corporate Governance after the Financial Crisis* (2012) 251.

²¹ See James McConville, 'Notes and Current Developments: Directors' Duties to Stakeholders: A Reform Proposal Based on Three False Assumptions' (2005) 18(1) *Australian Journal of Corporate Law* 88.

²² See Xavier Vives (ed), *Corporate Governance: Theoretical and Empirical Perspectives* (2000).

²³ For the study on corporate governance in the context of Thailand, see Deunden Nikomborirak, 'Building Good Corporate Governance After the Crisis: The Experience of Thailand' in Ho Khai Leong (ed), *Reforming Corporate Governance in Southeast Asia: Economics, Politics, and Regulations* (2005); Saravuth Pitayasak, 'National Corporate Governance Committee: Three Disciplines for Good Corporate

Chapter 3, the Stock Exchange of Thailand (SET) was the first to respond to the perceived weaknesses in corporate governance in Thai listed companies. In the beginning, the SET encouraged listed companies to establish audit committees to oversee the management. Later it amended its listing rules to require all listed companies to appoint such committees.²⁴ In 2001 its guidelines for good corporate governance were released, known as the *Report on Corporate Governance*.²⁵ One year later the *Report* was replaced by the *Principles of Good Corporate Governance*.²⁶ Although the guidelines had no formal legal status, under their contracts with the SET, listed companies had to comply with it or give reasons for not complying.²⁷ In 2004 the Thai Securities and Exchange Commission (“Thai SEC”) participated in the Reports on the Observance of Standards and Codes (ROSC) project initiated by the World Bank. This project aimed to evaluate the effectiveness of domestic corporate governance practices of the participating countries against the Organisation for Economic Co-operation and Development (OECD) standards. After the outcomes were published, the SET revised the *Principles of Good Corporate Governance* and then published the updated version of the code in 2006.²⁸ This version largely included the recommendations made by the World Bank in the ROSC project.²⁹ In addition to changes to the corporate governance code, Thai company law was significantly amended in 2008. New legal concepts, different from any previous ones in Thai law, such as shareholders’ proposals,³⁰ the business judgment rule,³¹ and proxy solicitation³² were introduced. The purpose of the amendments was to bring Thai law, regulations, and corporate governance practices into alignment with international standards. Following conventional principles, endorsed by international institutions and many legal and regulatory scholars, the Thai government is attempting to strengthen good

Governance in Thailand' in Ho Khai Leong (ed), *Reforming Corporate Governance in Southeast Asia: Economics, Politics, and Regulations* (2005).

²⁴ Stock Exchange of Thailand, *SET's Role* (2009) Stock Exchange of Thailand, <http://www.set.or.th/en/regulations/cg/roles_p1.html> at 20 March 2012.

²⁵ Stock Exchange of Thailand, *Report on Thai Corporate Governance* (2001).

²⁶ *The 15 Principles of Good Corporate Governance for Listed Companies* (2001).

²⁷ Stock Exchange of Thailand, *The Principles of Good Corporate Governance for Listed Companies* (2006) 3.

²⁸ *Ibid.*

²⁹ *Ibid.* 2.

³⁰ The discussion on shareholders’ proposals is in Chapter 4.

³¹ The discussion on the business judgment rule is in Chapter 5.

³² The discussion on proxy solicitation is in Chapter 4.

governance mechanisms in the belief that this will attract investors' interest.³³ The resulting investments, from both local and foreign sources, it could reasonably have been anticipated, would flow into its securities markets and spur further economic growth.³⁴

Although the reforms have been implemented, there are outstanding issues that still need to be addressed. Firstly, in exchange for the financial assistance provided by the International Monetary Fund (IMF), Thailand was required to commit to fundamental reforms of its corporate governance systems by applying OECD standards.³⁵ This model developed under the influence of Anglo-American commercial law and practice.³⁶ The US approach emerged from the ongoing separation of ownership and control. Listed companies in the US are generally held by a large number of small shareholders. Each of them has no control over the company. Such control is therefore vested in managers. Laws and the regulatory framework seek to ensure that the interests of shareholders are not exploited by the managers. However, as will be made clear, the conflicts of interests within Thai companies are not between managers and shareholders, but the controlling and minority shareholders. Thai companies are usually controlled by a limited number of majority shareholders. Majority shareholders can easily nominate the board members and dominate the shareholders' meetings. Given such a difference, it is questionable whether international standards based on US law can provide suitable protection for minority shareholders in Thai listed companies. As pointed out by many scholars, there are no principles or standards that can apply to all jurisdictions.³⁷

³³ David C Kang, 'Symposium on Enron, Worldcom, and their Aftermath: The Impact of Enron on Asian Business' (2003) 27 *Vermont Law Review* 909, 909–10.

³⁴ See Rafael La Porta et al, 'Investor Protection and Corporate Governance' (2000) 58 *The Journal of Financial Economics* 3, 16–7.

³⁵ The OECD Principles of Corporate Governance 2004. See Timothy Lane et al, *IMF-Supported Programs in Indonesia, Korea, and Thailand: A Preliminary Assessment* (1999) 18. The World Bank developed projects, based on the OECD standard, to assess the effectiveness of domestic corporate governance regimes such as the Reports on the Observance of Standards & Codes project. See World Bank, *ROSC: Reports on the Observance of Standards & Codes* (2009) World Bank, <http://www.worldbank.org/ifa/rosc_more.html> at 20 March 2012.

³⁶ The discussion on the separation of ownership and control is in Chapter 2.

³⁷ See Steve Letza, Xiuping Sun and James Kirkbride, 'Shareholding versus Stakeholding: A Critical Review of Corporate Governance' (2004) 12(3) *Corporate Governance: An International Review* 242, 253; Yuan Dujuan, 'Inefficient American Corporate Governance under the Financial Crisis and China's Reflections' (2009) 51(3) *International Journal of Law and Management* 139.

Secondly, transplanting legal concepts from other jurisdictions, or international standards based on them, into Thai law is not a simple task. Many comparative law scholars affirm that, given the different local contexts between donor and recipient jurisdictions, adopted rules cannot be easily transplanted.³⁸ In their view, law has a strong attachment to its surrounding social structures. Without a similar context, adopted rules may not function in similar ways in recipient jurisdictions.³⁹ Some principles can theoretically protect minority shareholders' interests but may not work in practice. Also principles that run contrary to Thai business practice may be rejected.⁴⁰ Alternatively adopted rules may interact with, or irritate the existing legal and regulatory systems and produce unexpected outcomes.⁴¹ Also, if local legal agents do not have a sufficient understanding of the adopted rules, they may misapply or ignore them.⁴²

The research project underlying this thesis is designed to identify the key principles of, and their application to, minority shareholders' protection in two potential donor jurisdictions, Germany and the United States. It also examines legal and regulatory principles for the protection of minority shareholders in the Thai legal and regulatory system. The issues of how, and to what extent, the regulatory frameworks used in those jurisdictions should be employed in Thailand are also part of the research. The research further considers ways to overcome obstacles to the effective implementation of corporate law reform in Thailand.

³⁸ See eg Baron De Montesquieu, *The Spirit of Laws* (Thomas Nugent trans, 1914). Watson on the contrary viewed 'the act of borrowing is usually simple'. Cf Alan Watson, 'Aspects of Reception of Law' (1996) 44 *American Journal of Comparative Law* 335, 335.

³⁹ See Katharina Pistor, 'The Standardization of Law and Its Effect on Developing Economies' (2002) 50 *The American Journal of Comparative Law* 97, 129; Troy A Paredes, 'A System Approach to Corporate Governance Reform: Why Importing US Corporate Law isn't the Answer' (2004) 45 *William & Mary Law Review* 1055, 1155; Pramuan Bunkanwanicha and Yupana Wiwattanakantang, 'Big Business Owners in Politics' (Working Paper No 2006-10, Center for Economic Institutions, Institute of Economic Research, Hitotsubashi University, 2007); Layna Mosley, 'Regulating Globally, Implementing Locally: The Future of International Financial Standards' (Working Paper, Centre for International Governance Innovation, 2008) 10.

⁴⁰ Walter pointed out the large gaps between formal rules and institutions, and actual policy and actual behaviour. Andrew Walter, *Governing Finance: East Asia's Adoption of International Standards* (2008).

⁴¹ The details on this argument are discussed in Chapters 3 and 8.

⁴² This issue is discussed further in Chapters 3 and 8.

1.2 Core research questions

As mentioned, the purposes of this study are to examine the concept of minority shareholders' protection in the Thai context, and to design a model for the reform of Thai law to promote minority shareholders' protection based on Thai legal, social, and economic circumstances. To achieve such aims, the research covers the following:

- (i) minority shareholders' protection in the present Thai legal and regulatory frameworks;
- (ii) the transplantation and implementing of principles from other legal frameworks into Thailand; and
- (iii) obstacles to implementing legal reforms in Thailand.

These issues are addressed in three research questions.

1.2.1 Does the Thai legal framework provide adequate protection for minority shareholders?

As the aim of this research is to evaluate and suggest reforms to minority shareholders' protection in Thailand, it is necessary to evaluate existing Thai laws and regulations. To determine their sufficiency in protecting minority shareholders' interests, the first consideration is which benchmark should be used. According to Mäntysaari, choosing the jurisdictions to be compared is vital.⁴³ He claimed that '... the work of the comparative lawyer is not meaningful unless the choice of jurisdictions is meaningful'.⁴⁴ It is accepted by scholars that there are no universally applicable standards or principles,⁴⁵ the research thus does not apply an international model, such as the OECD Principle of Corporate Governance as a benchmark, although it remains relevant. Instead, it searched for suitable principles and processes to be adopted in

⁴³ Petri Mäntysaari, *Comparative Corporate Governance: Shareholders as a Rule-maker* (2005) 10.

⁴⁴ Ibid 10.

⁴⁵ Paredes, above n 39; 1155; Pistor, above n 39; 129; Mosley, above n 39, 10. See also Layna Mosley, 'Attempting Global Standards: National Governments, International Finance, and the IMF's Data Regime' (2003) 10(2) *Review of International Political Economy* 331; Layna Mosley, 'An End to Global Standards and Codes?' (2009) 15 *Global Governance* 9.

Thailand. It focuses on US and German legal principles as possible sources of ideas to be used in legal reform in Thailand.

Using US law as a comparator and possible source is appropriate as, similarly to other Asian countries, Thailand has been under considerable pressure to follow laws and regulations which derive from the US.⁴⁶ After the 1997 financial crisis, Thailand was required by the IMF and the World Bank to commit to corporate governance restructuring and apply the OECD standards as the preferred model. Those standards on corporate governance are broadly based on Anglo-American commercial law and business practice.⁴⁷ It has been claimed that the domestic and international success of the US indicates the highest point in the evolution of law and regulation.⁴⁸ Additionally, the studies of La Porta *et al* on the relationship between law and economic development suggest that common law jurisdictions, especially the US, have stronger legal protection for investors than civil law jurisdictions.⁴⁹ Consequently, it is claimed, developing economies should harmonise their laws with US law to enable the development of sound and stable financial markets.⁵⁰ On the other hand, although their publications are amongst the most cited in the past decade, they are also heavily criticised.⁵¹ Siems argued that there was a home bias problem in their methodology.⁵² He claimed that they made assumptions, primarily based on common law concepts in general and US law in particular, in evaluating foreign legal systems.⁵³ Siems further pointed out that they

⁴⁶ Pasuk Phongpaichit and Chris Baker, *Thailand's Crisis* (2000) 37–8.

⁴⁷ Mosley, above n 39, 3. Ruth V Aguilera and Alvaro Cuervo-Cazurra, 'Codes of Good Corporate Governance Worldwide: What is the Trigger?' (2004) 25(3) *Organization Studies* 415, 436.

⁴⁸ Ronald J Gilson, 'Globalizing Corporate Governance: Convergence of Form or Function' (2001) 49(2) *The American Journal of Comparative Law* 329, 331.

⁴⁹ See Rafael La Porta et al, 'Investor Protection and Corporate Valuation' (2002) 57 *The Journal of Finance* 1147. In 1937, Hayek held a similar view: '... the ideal of individual liberty seems to be [flourishing] chiefly among people where, at least for long periods, judge-made law predominated'. Friedrich Hayek, *Law, Legislation, and Liberty: A New Statement of the Liberal Principles of Justice and Political Economy* (1937) 94.

⁵⁰ Pistor, above n 39, 103–4.

⁵¹ See Paul G Mahoney, 'The Common Law and Economic Growth: Hayek Might be Right' (2001) 30 *The Journal of Legal Studies* 503; David Donald, 'Approaching Comparative Company Law' (2008–2009) 14 *Fordham Journal of Corporate & Financial Law* 83, 92–3; Ralf Michaels, 'Comparative Law by Numbers? Legal Origins Thesis, Doing Business Reports, and the Silence of Traditional Comparative Law' (2009) 57 *American Journal of Comparative Law* 765; Christopher A Whytock, 'Legal Origins, Functionalism, and the Future of Comparative Law' (2009) 2009 *Brigham Young University Law Review* 1879.

⁵² Mathias M Siems, 'What Does Not Work in Comparing Securities Laws: A Critique on La Porta et al's Methodology' (2005) *International Company and Commercial Law Review* 300.

⁵³ *Ibid* 301.

observed only the legal similarities and differences without considering their historic, social, cultural, and economic contexts.⁵⁴ Ramsay *et al* have sought to further refine the methodology used so that it is more discriminative of, and, attentive to differences and similarities across legal systems.⁵⁵ On the other hand, Milhaupt and Pistor in the mid-2000s studied the rolling relationships between legal and economic developments in the US, Germany, Japan, South Korea, China, and Russia.⁵⁶ They found that ‘no single type of legal system is uniquely associated with economic success’.⁵⁷ The current global financial crisis also raises the question of whether the adaptation of US laws and regulations is still appropriate. The failures of both US and transnational corporations have revealed the weaknesses inside US companies and the high level of self-regulation emphasised in the US corporate governance system.⁵⁸

Consequently, this research also considers the German legal model as another benchmark to measure the effectiveness of the Thai legal framework on minority shareholders’ protection. German law and practice may be a better source for Thailand as Thai law has been largely influenced by the German legal system. According to Berkowitz *et al*, for practical implementation, legal policies and rules should be borrowed from a jurisdiction with a similar legal heritage so that domestic legal agents will be familiar with the imported laws.⁵⁹ Furthermore, the structures of Thai and

⁵⁴ Ibid 303.

⁵⁵ Helen Anderson, Michelle Welsh, Ian Ramsay, and Peter Gahan, 'The Evolution of Shareholder and Creditor Protection in Australia: An International Comparison' (2012) 61 *International and Comparative Law Quarterly* 171, 176-181.

⁵⁶ Curtis J Milhaupt and Katharina Pistor, *Law and Capitalism: What Corporate Crises Reveal about Legal Systems and Economic Development Around the World* (2008). In the Thai context, a rolling relationship between law and economics is also found. The discussion is in Chapter 3.

⁵⁷ Ibid 220; See also Katharina Pistor, 'Rethinking the "Law and Finance" Paradigm' (2009) 2009 *Brigham Young University Law Review* 1647. *Contra* La Porta *et al* in their article argued that there was a relationship between securities law and stock market development. Rafael La Porta *et al*, 'What Works in Securities Laws?' (2006) 61(1) *The Journal of Finance* 1. Donald Tsang, the Hon Chief Executive of Hong Kong, affirms that '[t]here is no "one-size-fits-all" model of economic development, given the varying socio-economic background and needs of individual economics'. Donald Tsang, 'Opening Remarks' (Speech delivered at the Regulating Global Economy for Global Growth, Hong Kong, 12 November 2009).

⁵⁸ Office of the Press Secretary, *Declaration of the Summit on Financial Markets and the World Economy* (2008) The White House, President George W Bush, <<http://www.iasplus.com/en/binary/crunch/0811g20declaration.pdf/view>> at 20 March 2012; The Monetary and Capital Markets Department, *Lessons of the Financial Crisis for Future Regulation of Financial Institutions and Markets and for Liquidity Management* (2009) International Monetary Fund, <<http://www.imf.org/external/np/pp/eng/2009/020409.pdf>> at 20 March 2012.

⁵⁹ Daniel Berkowitz, Katharina Pistor and Jean-Francois Richard, 'Economic Development, Legality, and the Transplant Effect' (2003) 47 *European Economic Review* 165.

German firms both similarly reflect concentrated ownership.⁶⁰ Given these similarities, the thesis considers how German company law and regulatory practice can be used as an alternative approach for Thailand.

1.2.2 Is the transplantation of the legal frameworks applied in other jurisdictions into Thailand feasible?

The study of comparative law is the comparison of different legal systems.⁶¹ It not only contrasts the texts of laws from two or more different jurisdictions but also extends to considering the legal cultures and histories of the jurisdictions compared.⁶² The rise of comparative legal studies began when Montesquieu in the 18th century, considered the influence of geography and culture on law in different countries.⁶³ Comparative law as a contemporary academic study started in Paris in 1900. It was largely expanded by two French scholars, Édouard Lambert and Raymond Saleilles, who founded the International Congress for Comparative Law.⁶⁴ In the late 19th century, the study of the reception of legal principles became a central issue in comparative law following the much earlier reception of Roman law in Europe.⁶⁵ One of the Congress's sessions, held in 1970, was on the Global Reception of Foreign Law. Four years later, the concept of legal transplants became a critical theme in comparative law, particularly in Watson's work.⁶⁶ A core question in the research for this thesis is whether legal concepts or rules from one legal system may be effectively adopted into another. The comparative law literature reveals a fundamental disagreement over the feasibility of transplants.

⁶⁰ See Stijn Claessens, Simeon Djankov and Larry HP Lang, 'Who Controls East Asian Corporations?' (Policy Research Working Paper No 2054, World Bank, 1999); Julian R Franks and Colin Mayer, 'Ownership and Control of German Corporations' (2001) 14(4) *Review of Financial Studies* 943.

⁶¹ Konrad Zweigert and Hein Kötz, *Introduction to Comparative Law* (Tony Weir trans, 3rd revised ed, 1998) 2.

⁶² Michele Graziadei, 'Comparative Law as the Study of Transplants and Receptions' in Mathias Reimann and Reinhard Zimmermann (eds), *The Oxford Handbook of Comparative Law* (2006) 442.

⁶³ See Montesquieu, above n 38.

⁶⁴ Zweigert and Kötz, above n 61, 2.

⁶⁵ Graziadei, above n 62, 442.

⁶⁶ One of these influential works is Alan Watson, *Legal Transplants: An Approach to Comparative Law* (1974).

Watson, a leading scholar in comparative law, argued that the fruitful source of legal change is borrowing and 'the act of borrowing is usually simple'.⁶⁷ He further suggested that although legal rules were part of the social structure, their origin was not the 'inevitable consequence of the social structure'.⁶⁸ The transplantation of foreign rules began when those who had control over the law making process believed that such transplantation would be beneficial.⁶⁹

Other scholars viewed this issue differently. They held that legal rules could not be easily transplanted from one legal system to another as they are deeply attached to the social structures. Montesquieu claimed that there is a link between laws and environmental, geographical, sociological, economic, cultural, and political characteristics, and therefore borrowed laws could not be easily fitted into the local circumstances of recipient jurisdictions.⁷⁰ He further explained that laws are not limited themselves to have not confined themselves to what is read as text but also extend to the spirit behind them. As he remarked, *l'esprit des lois* (the spirit of the laws) is 'a compound of physical, cultural, and political ingredients'.⁷¹ Kahn-Freund, following Montesquieu, affirmed that problems and failures would occur when legal transplantation took place without considering the different social and political circumstances of the donor and the recipient.⁷² In this context, transplanting legal rules from one system into another system may not be as simple as is indicated by Watson. Also contrary to Watson's approach, Legrand claimed that legal transplants could not happen.⁷³ The rules in the donor jurisdictions could not represent the same ideas as

⁶⁷ Watson, above n 38, 335.

⁶⁸ Alan Watson, 'Comparative Law and Legal Change' (1978) 37 *Cambridge Law Journal* 313, 315; for instance, in terms of the development of civil law, he claims that it is 'the result of purely legal history, and can be explained without reference to social, political, or economic factors'. See also William Ewald, 'Comparative Jurisprudence (II): The Logic of Legal Transplants' (1995) 43 *The American Journal of Comparative Law* 489, 500.

⁶⁹ Alan Watson, 'Legal Transplants and Law Reform' (1976) 92 *Law Quarterly Review* 79, 79.

⁷⁰ For a summary of Montesquieu's influence on the problem of transplanting legal institutions, see Otto Kahn-Freund, 'On Uses and Misuses of Comparative Law' (1974) 37(1) *The Modern Law Review* 1, 7.

⁷¹ *Ibid.*

⁷² *Ibid* 27.

⁷³ Pierre Legrand, 'What "Legal Transplants"?' in David Nelken and Johannes Feest (eds), *Adapting Legal Cultures* (2001) 63. See also Pierre Legrand, 'The Impossibility of "Legal Transplants"' (1997) 4 *Maastricht Journal of European and Comparative Law* 111; Pierre Legrand, 'The Same and the Different' in Pierre Legrand and Roderick Munday (eds), *Comparative Legal Studies: Traditions and Transitions* (2003) 240.

those in the borrowing countries.⁷⁴ According to him, ‘meaningful legal transplants’ can only occur when both the ‘propositional statement’ and its ‘invested meaning’ are transported.⁷⁵ However, this is unlikely to happen as the invested meaning, incorporated in the rule, is itself culture specific.⁷⁶ He concluded that ‘a crucial element of the ruleness of the rule – its meaning – does not survive the journey from one law to another’.⁷⁷ This literature clearly reflects considerable doubt about the feasibility of legal transplants.

Nevertheless, attempts by one legal system to adopt a particular solution from another legal system remain determined. The legal adoption of Western European legal systems in Asia provides a clear example. Thailand, for example, with a strong political will to regain judicial sovereignty, created a westernised legal order by adopting French and German law.⁷⁸ Currently, Thai legal reformers have adopted a number of Western legal concepts in the hope that they would bring similar economic growth and development as they have in Western jurisdictions. Although Thailand has been adopting foreign laws for 130 years, the research on legal transplants in the Thai context remains very limited. Thai legal history has dealt with it but the issues of how the adopted rules have been incorporated into the Thai legal system and culture have not been extensively studied. One of the pioneers of such studies, Chomchai has urged:

For the sake of possible institutional reform in Thailand and to make it possible for Thai academics to undertake comparative research on the legal system ... there is an urgent need for Thai academics, which lag far behind, to catch up.⁷⁹

Summing up, the transplanting of legal rules requires a complete understanding of both laws and local contexts of the donor and recipient jurisdictions. It is also necessary to bear in mind that transferring rules or concepts from one jurisdiction to another may entail the risk of rejection or the transformation of the legal principle by it being be used

⁷⁴ Legrand, above n 73, 63–4.

⁷⁵ Ibid 60.

⁷⁶ Ibid.

⁷⁷ Ibid.

⁷⁸ See Chapter 8 for a detailed discussion.

⁷⁹ Prachoom Chomchai, 'Editor's Introduction, Acknowledgements and Disclaimer' in Prachoom Chomchai (ed), *Development of Legal Systems in Asia: Experiences of Japan and Thailand* (1997) 61.

in another way.⁸⁰ The research considers some of the differences between the backgrounds of US, German, and Thai company laws and regulations. It also explores the social, economic and historical contexts of the emergence and use of minority shareholders' protection in the US and Germany. To determine whether the pattern of law found in these countries is able to be transplanted into the Thai legal and regulatory systems to strengthen them, the research uses the propositions made by Zweigert and Kötz. They suggested that there are two critical issues to consider in the adoption of a foreign legal solution: whether it has proved satisfactory in the jurisdictions from which it comes and whether it will work in the jurisdictions in which it is transplanted.⁸¹

1.2.3 What are the obstacles to legal reform in Thailand?

As earlier indicated, although law reform by transplanting legal principles is not unusual, successful reform is not easy to achieve. The experiences of other jurisdictions signal the difficulties faced by legal transplants in Thailand. In Japan, for example, Rokumoto pointed out that some domestic issues impeded legal reforms, including Japanese political and judicial 'infrastructures', resistance from legal agents, and the perceived negative impact of the legal reform on Japanese culture and society.⁸² As legal reform heavily relied on political policies, the readiness of political institutions and parties to respond positively to each step of the reform was necessary.⁸³ Although a positive change to the law might be made, it was unlikely to be successful if affected people did not cooperate in the proposal or its implementation.⁸⁴ In terms of the relationship between law reform and culture, he claimed that 'the reform of the legal system is a fight against culture'.⁸⁵ Culture, in his definition, was not limited to the culture of a particular group, such as the legal profession, but also included that of the large community.⁸⁶

⁸⁰ Kahn-Freund, above n 70, 27; see Kahei Rokumoto, 'Law and Culture in Transition' (2001) 49(4) *The American Journal of Comparative Law* 545.

⁸¹ Zweigert and Kötz, above n 61, 17.

⁸² Rokumoto, above n 80, 558–9.

⁸³ Ibid 558.

⁸⁴ Ibid.

⁸⁵ Ibid 559.

⁸⁶ Ibid.

Following Watson's remark on the importance of interest groups and agents,⁸⁷ the research considers the key obstacles to legal reform in Thailand by examining groups promoting and resisting legal reforms in Thailand in the context of better protecting minority shareholders. Obstacles may exist in both the public and private sectors. In the public sector, for instance, relevant Thai regulators and governmental agencies may not be familiar with or understand the proposed imported rules. They may misapply them or not be able to effectively implement and enforce them. In the private sector, the directly affected Thai business community may hinder the reform by exercising its control over the political system. When introduced, the controlling shareholders may resist the implementation of principles promoting better governance at the firm level. These are issues which have not been widely studied in Thailand and, as the conclusion of the thesis acknowledges, more research on them needs to be undertaken.

In Asian jurisdictions, it is generally thought that laws that meet internationally recognised standards are required. Yet there are limitations on the introduction and implementation of such laws in national legal systems. Change to existing national law is often difficult and also a time-consuming process. The legal system does not stand alone but connects to the economic and political systems.⁸⁸ The objectives of legal reform cannot be achieved without concern for all related systems and institutions. Furthermore, to implement the proposed legal rules, their potential to be enforced is vital. In the absence of effective enforcement, corporate managers or directors will ensure that principles of corporate law and governance remain only law in the book.⁸⁹ A number of writers affirm that one of the weaknesses in Asian legal systems is the dysfunction in legal enforcement.⁹⁰ The research examines the weaknesses in the Thai legal and regulatory systems relating to enforcement. The consideration of these

⁸⁷ Watson, above n 68, 315.

⁸⁸ Aguilera and Cuervo-Cazurra, above n 47. This view is similar to Luhmann's system theory that suggests that law has a special relationship to its environment. Law is different from its environment but it could not exist without the environment. See Niklas Luhmann, *Law as a Social System* (Klaus A Ziegert trans, 2004); Andreas Philippopoulos-Mihalopoulos, *Niklas Luhmann: Law, Justice, Society* (2009); Christian Borch, *Niklas Luhmann* (2011); Christian Borch, *Niklas Luhmann* (2011).

⁸⁹ John Fagan, 'The Role of Securities Regulation in the Development of the Thai Stock Market' (2003) 16 *Columbia Journal of Asian Law* 303.

⁹⁰ Rafael La Porta et al, 'Law and Finance' (1998) 106(6) *Journal of Political Economy* 1113, Table 5; Stijn Claessens and Joseph PH Fan, 'Corporate Governance in Asia: A Survey' (2002) 3(2) *International Review of Finance* 71, 5.

obstacles to legal reform is important in providing a fundamental understanding of how to provide better protection for minority shareholders.

1.3 Research methodology

1.3.1 Research design

The three-core research problems, mentioned in Section 1.2, indicate that this is a comparative law study and comparative law methodologies have been used. This research followed De Cruz's method of comparison.⁹¹ The problems of the thesis were precisely identified in the research questions. The parent legal family of the jurisdiction being compared was also specified. The primary and secondary sources were selected and gathered. The researcher then organised the materials in accordance with the legal philosophy and ideology of the legal systems being investigated. From the materials, the researcher mapped out the possible answers to the research questions. The legal principles were analysed based on their cultural meaning rather than literal meaning. The researcher finally formed conclusions with any critical commentary relating to the original purpose of the research questions.

As indicated, the literature is in two parts – primary and secondary. The primary sources include legislation, regulations, case law, and listing rules. In respect of the US, given the different jurisdictions within its federation, the corporate law of Delaware⁹² is chosen. This is because a large number of publicly held corporations are incorporated there.⁹³ The New York Stock Exchange (NYSE) listing rules are selected because they have been influential. The NYSE is the world's largest stock exchange by market capitalisation.⁹⁴ While analysing the primary sources – legislation and case law – the research bears in mind that the role of legislation and case law in civil and common law

⁹¹ Peter De Cruz, *Comparative Law in a Changing World* (2nd ed, 1999) 235–9.

⁹² Delaware General Corporation Law.

⁹³ The website of Delaware's Division of Corporations recites that '[m]ore than 850,000 business entities have their legal home in Delaware including more than 50% of all US publicly-traded companies and 63% of the Fortune 500.' *Division of Corporations* (2011) State of Delaware <<http://www.corp.delaware.gov/>> at 20 March 2012.

⁹⁴ *Time Series* (2010) World Federation of Exchanges <<http://www.world-exchanges.org/statistics/time-series>> at 20 March 2012.

jurisdictions differs. Civil law systems employ the statute as the primary source of law. Civil law judges interpret the text of a statute on a case-by-case basis. On the other hand, common law judges have had a significant role in promulgating law. The judges are entitled to define the scope of law through the decisions given. They are bound by previous decisions – *stare decisis*. However, the differences between common law and civil law systems have become blurred. In common law countries judicial decisions are no longer the main source of law as the number of statutes is growing significantly. In respect of case law, civil law systems also recognise the potential binding force of previous decisions through the principle of *jurisprudence constante*.⁹⁵ Landskron found no differences in the attitudes of judges to statutory interpretation in the civil and common law jurisdictions he studied.⁹⁶ Despite the apparent convergence, the researcher acknowledged these issues and analysed the data with caution.

In addition to the primary sources, secondary sources were utilised. Journals, reports, legislative histories, media, and websites were collected for analysis. The sources also include reviews, professional practices and commentaries on relevant laws as well as literature in scholarly monographs and serials.⁹⁷ The process of analysing relevant secondary data is through a form of coding. The relevant literature was considered how it related to the research questions. The analysis also considered how the selected literature informed the answers to the research questions and collected the concepts emerging from the literature. This research methodology allowed the researcher to employ a wide range of literature to compare the different approaches in dealing with minority shareholders' protection in the selected jurisdictions.

Together with the evaluation of Thai law on protecting minority shareholders, the research also seeks to answer the question of whether a pattern of law on minority shareholders' protection developed in the US and Germany can be incorporated into the Thai legal system. This requires looking beyond the laws in statute-books to understand the development and evaluate the practical application of such laws. It draws mainly on

⁹⁵ Max Rheinstein, 'Common Law and Civil Law: An Elementary Comparison' (1952–1953) 22 *Revista Juridica de la Universidad de Puerto Rico* 90, 96.

⁹⁶ Rolf Landskron, *Common-law and Civil-law Legal Families: A Misleading Categorisation* (M Laws Thesis, Bond University, 2008).

⁹⁷ De Cruz, above n 91, 236-7.

legal literature but includes perspectives from economics, history, sociology, and political science. The secondary literature on the reception of foreign law into the Thai legal system was reviewed to provide a historical background and an understanding of Thai legal culture. While the literature dealing with minority shareholders' protection provides the academic point of view on this issue, the direct experience of those working in this field is necessary to understand the law in practice. The opinion of practitioners is also insightful on whether the theoretical concepts and adopted rules can be functional in practice. Further, their views help to reveal the gaps in the Thai legal system on minority shareholders' protection and this may lead to suggestions on its improvement.

A qualitative research methodology is considered as the most appropriate method for the research questions. According to Denzin and Lincoln, qualitative research is:

[A] situated activity that locates the observer in the world. It consists of a set of interpretive, material practices that make the world visible. These practices transform the world. They turn the world into a series of representations ... At this level, qualitative research involves an interpretive, naturalistic approach to the world. This means that qualitative researchers study things in their natural settings, attempting to make sense of, or interpret phenomena in terms of the meanings people bring to them.⁹⁸

The qualitative method is one of two major social sciences research methodologies – qualitative and quantitative. Unlike the quantitative method, qualitative studies do not examine quantity, amount, intensity or frequency of data.⁹⁹ Qualitative research methods facilitate an in-depth understanding of a particular issue because it allows more open-ended questions and explanations than quantitative methods which seek an answer to a given question in order to generalise the outcomes of the findings to a wider population.¹⁰⁰ Qualitative research focuses on the nature of reality and seeks answers to questions of how social experience is created and its meaning to human beings.¹⁰¹ It

⁹⁸ Norman K Denzin and Yvonna S Lincoln, 'The Discipline and Practice of Qualitative Research' in Norman K Denzin and Yvonna S Lincoln (eds), *Handbook of Qualitative Research* (2nd ed, 2000) 1, 3.

⁹⁹ Ibid 8.

¹⁰⁰ Sharlene Hesse-Biber and Patrica Leavy, 'Distinguishing Qualitative Research' in Sharlene Hesse-Biber and Patrica Leavy (eds), *Approaches to Qualitative Research* (2004) 1, 2–6; Sharlene Hesse-Biber, *Mixed Methods Research: Merging Theory with Practice* (2010) 63–4.

¹⁰¹ Denzin and Lincoln, above n 98, 8.

also enables a researcher to build a close relationship with what is studied.¹⁰² The qualitative method is suitable for this research as it assists in the understanding and examination of the context of law in society.¹⁰³ By employing this research method, the researcher may collect and analyse personal opinions based on their experience of how the law functions in practice, and its consequences on society.¹⁰⁴

Qualitative research processes are varied. They include a number of empirical materials such as observations, in-depth interviews, group interviews, and case studies. The researcher employed the semi-structured in-depth interview method. In-depth interviews are the most commonly used approach in qualitative research.¹⁰⁵ This method allows the researcher to select appropriate participants, set up an interview schedule, and, during the interview, encourage respondents to explain their views and to provide concrete examples or empirical experiences.¹⁰⁶ The information gained from the interviewees does not limit itself to only their experiences but extends to the time of the interview and their views on what is going to happen.¹⁰⁷ The face-to-face communication enables the researcher to capture ‘an insight into the experiences, concerns, interests, beliefs, values, knowledge, and ways of seeing, thinking and acting’ of the interviewees.¹⁰⁸ The interview method suited this research as it also allowed the researcher to gather the information from people experienced with Thai corporate governance and regulatory practices. Unlike the structured interview, the semi-structured interviews allowed the researcher to use an interview schedule as a guideline rather than be dictated by it.¹⁰⁹ This facilitated greater flexibility in what was covered and a chance to introduce issues which had not been thought of and ask following up questions.¹¹⁰ This method, however, has a particular weakness. The interview data gives the observations on the personal beliefs and judgments of a limited number of selected interviewees rather than

¹⁰² Ibid.

¹⁰³ Terry Hutchinson, *Research and Writing in Law* (2006) 88.

¹⁰⁴ Michael Quinn Patton, *Qualitative Research & Evaluation Methods* (3rd ed, 2002) 16–21.

¹⁰⁵ Yvonne Darlington and Dorothy Scott, *Qualitative Research in Practice: Stories from the Field* (2002) 48.

¹⁰⁶ See Hutchinson, above n 103, 102.

¹⁰⁷ Darlington and Scott, above n 105, 50.

¹⁰⁸ John F Schostak, *Interviewing and Representation in Qualitative Research* (2006) 10.

¹⁰⁹ Jonathan A Smith, 'Semi-structured interviewing and Qualitative Analysis' in Jonathan A Smith, Rom Harre and Luk Van Langengrove (eds), *Rethinking Methods in Psychology* (2005) 9.

¹¹⁰ Ibid 9–11; John M Johnson, 'In-Depth Interviewing' in Jaber F Gubrium and James A Holstein (eds), *Handbook of Interview Research: Context and Method* (2001) 105–7.

the facts.¹¹¹ Possibly what people say in the interview may not be what they do, or may not be the whole truth. Unlike the quantitative method mainly based on statistics, interviews also do not generate concrete data. The author recognises these criticisms but believes that this research method yields insightful information of significant value to the project. To date, there has been little similar empirical research. This field work, therefore, provides a first-hand and deeper understanding of minority shareholders' protection in Thailand.

1.3.2 Preparation of the interviews

Before conducting the interviews, the author designed an interview schedule based on issues identified in the literature review. This process is important as, in producing the schedule, the researcher reflected on which issues to discuss and how the questions in the interview schedule relate to the research questions. While drafting the interview schedule, the author gave some thought to what may happen during the interviews and any difficulties that may occur. The issues of word choice and sensitive topics were also considered. The language used in the interview schedule proved easy for the interviewees to understand and immediately respond to. The questions in the schedule are neutral and open-ended. The interview schedule¹¹² was drafted in 2009 and reviewed by Professor Neil Andrews, the supervisor of this thesis, and Victoria University Human Research Ethics Committee.

In addition to constructing the interview schedule, the process of selecting participants was conducted. As one of the main objectives of the interviews was to improve the understanding of minority shareholders' protection in Thailand, the participants were those with considerable experience in Thai corporate governance. Potential participants were recruited in Thailand. A purposive sampling method was applied in determining interviewees among a great number of organisations and people related to minority shareholders' protection. To ensure the credibility of the interview, the selection of

¹¹¹ Ashley Black, 'The Reform of Insider Trading Law in Australia' (1992) 15 *The University of New South Wales Law Journal* 214, 218.

¹¹² See Appendix A for the interview schedule. The schedule is based, in part, on a schedule designed by Professor Roman Tomasic and Professor Neil Andrews in 2004 to investigate corporate governance practice in Chinese listed companies.

interviewees was based on their experiences and knowledge of minority shareholders' protection. According to Holloway, the sample size generally is between four to forty participants.¹¹³ However, the number of samples was reviewed during the research to ensure that it was as comprehensive as possible and to deal with saturation. As indicated below, 21 participants were interviewed in this study.

To gain opinions from varied perspectives, the interviewees were chosen from different occupational groups, such as directors, lawyers, judges, prosecutors, regulatory officers, stock exchange officers, financial analysts, and academics. The viewpoints of the professional independent directors reflected the perspective of the management on minority shareholders' protection. In addition, issues of the relationships between minority shareholders and controlling shareholders and between minority shareholders and directors were raised during the interviews with independent directors. The interviews with corporate lawyers, accountants and financial analysts were particularly beneficial to the research. Their experience of working with Thai listed companies provided a deeper understanding of Thai business practice, corporate culture, as well as their roles in practice. Representatives from a number of non-governmental organisations that are directly related to the protection of minority shareholders, such as the Thai Investors Association and the Thai Institute of Directors Association, were also interviewed to evaluate their roles in protecting minority shareholders. Sophisticated investors were chosen to provide their views on the Thai capital market. In the case of regulatory authorities, the interviews were conducted with officers of the Stock Exchange of Thailand and the Securities and Exchange Commission of Thailand to expand the information on how the Thai capital market is supervised and regulated. In addition to these supervisory organisations, law enforcement agencies also play significant roles in implementing the legal rules. Interviewees therefore included a selection of judges, public prosecutors, and investigatory authorities that are involved in corporate and securities litigation. As cases brought to Thai courts are rare, the views of the law enforcement agencies on the obstacles to law enforcement in Thailand are particularly valuable. A number of legal academics from major university law schools were also interviewed.

¹¹³ Immy Holloway, *Basic Concepts for Qualitative Research* (1997).

In all, interviewees can be classified into two broad categories as follows:

Category A: Private sector

- i. Professional independent directors
- ii. Non-governmental organisations, such as the Thai Investors Association and the Thai Institute of Directors Association
- iii. Corporate lawyers
- iv. Accountants
- v. Financial analysts
- vi. Investors

Category B: Public sector

- i. Judges
- ii. The public prosecutor and investigatory authorities
- iii. The Securities and Exchange Commission of Thailand
- iv. The Stock Exchange of Thailand
- v. Academic researchers

The potential participants were firstly contacted by email in November 2009. However, no responses were received. Presumably the selected potential participants, who hold senior positions, were too busy to be available or willing to participate. The author therefore decided to seek help from her colleagues, former professors, friends, and family members in contacting these potential participants to draw their attention to the emails again. The use of such connections benefited the research as, given the various people and organisations they had connections with, the range of potential interviewees was not limited to a particular group. The author had the chance to briefly discuss the research and the interviews with the selected participants. After having them agree on the time and date for the interviews, only a few interviewees asked to see the interview schedule in advance. When this occurred it was through the personal assistants of the interviewees in order to enable the interviewees to prepare for the interviews. However, at the interviews, the author found that, due to their tight schedules, the interviewees stated that they had no chance to look at the interview questions in advance.

1.3.3 Conduct of the interviews

The 21 interviews commenced on 15 December 2009 and the final interview was conducted on 18 February 2010. The locations of the interviews were selected by each participant. All of the interviews were carried out in the offices of the interviewees. At the beginning of each interview, although the participants had an understanding of the research, the author explained the nature of the research and the scope of the interview. Each interviewee was given *Information to Participants Involved in Research*,¹¹⁴ which contains the details of the research and the interviews. The document was approved by Victoria University Human Research Ethics Committee. The author gave them sufficient time to read through the document. In addition, the author further informed the interviewees that they could withdraw from the interviews any time without prejudice. Concerning confidentiality, the interviewees were informed that the information given during the interviews was to be used only in the thesis and their responses would remain confidential. The interviewees would not be named as having participated in the research project. The researcher asked the interviewees' permission to have the interview digitally recorded.¹¹⁵ All interviewees allowed the use of a recorder. This benefited the research as the interviewer could fully concentrate on the interviews rather than taking notes. Before conducting the interviews, the author also ensured that *Consent Form for Participants Involved in Research*¹¹⁶ was read and signed.

The length of each interview varied and generally lasted between one to two-and-a-half hours. Most of the interviewees had previous experience in giving an interview to the media so their answers were relatively clear and concise. The interview schedule was used to ensure that the relevant issues were discussed. However, some variations were made during the interviews in accordance with the particular experience and knowledge of the interviewees and the responses gained from previous interviewees.

¹¹⁴ See Appendix B for the Information to Participants Involved in Research.

¹¹⁵ In case of objections, notes would have been taken during the interview and written up immediately afterwards.

¹¹⁶ See Appendix C for Consent Form for Participants Involved in Research.

According to Monahan and Fisher, a significant factor that may affect the result of the interviews is 'observer effect'.¹¹⁷ Due to the presence of a researcher, the interviewees may behave differently from their usual manner while being interviewed. The information they gave may also be different from what they actually have in mind. The factors related to such an effect include age, class, hierarchy, and status of the interviewer and the respondents.¹¹⁸ Denzin pointed out that the different genders of the interviewer and the interviewee, for example, make a difference to the interview because the cultural boundaries and identities of males are different from those of females.¹¹⁹ As well, respondents of a higher status may be accustomed to being in control of others and asking, rather than answering, questions. The researcher attempted to minimise this effect by maintaining a friendly, courteous, conversational, and professional manner. Before the interviews, the researcher believed that the core difficulty of the interviews would be the difference in status between the interviewer and the interviewees. Such a difference may prevent the building of rapport between the interviewer and the respondents.¹²⁰ The researcher found that all the interviewees were friendly, helpful, and responsive. Some interviews were more formal than others. This mainly depended on the personality of the interviewees rather than whether they came from the private or public sector, or to which organisations they belong. The researcher maintained a tone of friendly conversation but remained close to the interview schedule. The participation by the interviewer in each interview differed. The connection between interviewer and interviewees in some interviews was easy to establish and this made the discussion more active. The interviewer, however, limited her interaction to ensure that the interviews were not disrupted. Regardless of their occupations, the interviewees appeared to give opinions without constraints. This may be because the participants had had a long experience in this area so they had the confidence to reflect their views in a straightforward way. Immediately afterwards, the interviews were transcribed to be read and analysed. The interviewer also made observations of the interviewees, particularly

¹¹⁷ See Torin Monahan and Jill A Fisher, 'Benefits of "Observer Effects": Lessons from the Field' (2010) 10(3) *Qualitative Research* 357.

¹¹⁸ Irving Seidman, *Interviewing as Qualitative Research* (1991).

¹¹⁹ Norman K Denzin, *The Research Act: A Theoretical Introduction to Sociological Methods* (3rd ed, 1989) 116.

¹²⁰ Nigel King and Christine Horrocks, *Interviews in Qualitative Research* (2010) 56–7.

her perception of the level of their experience, knowledge and veracity and also indicating institutional points of view or conflicts of interest they may have.

1.3.4 Application of the research material

According to Basit, an analysis of qualitative data is not a separate self-contained phase and can start as soon as the data is available.¹²¹ The researcher therefore began the analysis with the first interview by considering what information had been given and what had been omitted.¹²² The transcripts of the interviews were used to evaluate the results of the interviews. While reading through the transcripts, the author annotated them to point out: how the answers were related to the research questions; how the answer to one question related to others; and, whether the author agreed with the answer as the basis of other data, etc.¹²³ The answer to the first question was significant in interpreting the others as it reflected the viewpoint of the interviewees regarding how important the concept of minority shareholders' protection was to them. The author found that in each reading there were some new ideas emerging. After a number of readings, the major themes of the interviews were identified by coding.

Richards explains that coding is 'not merely to label all the parts of documents about a topic, but rather to bring them together so that they can be reviewed, and your thinking about the topic developed'.¹²⁴ Similar ideas were clustered under the same theme title.¹²⁵ In a theme, there were also a number of categories.¹²⁶ The author also crossed checked among the themes to ensure that all themes were comparable.¹²⁷ Once the master list of the themes was produced, the author read through the transcripts again to check whether the themes were correctly identified. The common themes included: the strengths and weaknesses of family-owned companies, Thai business practices, the

¹²¹ Tehmian N Basit, 'Manual or Electronic? The Role of Coding in Qualitative Data Analysis' (2003) 45(2) *Educational Research* 143, 152.

¹²² Herbert J Rubin and Irene S Rubin, *Qualitative Interviewing: The Art of Hearing Data* (2005).

¹²³ See Smith, above n 109, 19.

¹²⁴ Lyn Richards, *Handling Qualitative Data: A Practical Guide* (2nd ed, 2009) 94.

¹²⁵ This concept is commonly recognised as 'thematic analysis'. See William J Gibson and Andrew Brown, *Working with Qualitative Data* (2009) 128–130.

¹²⁶ See Catherine Marchall and Gretchen B Rossman, *Designing Qualitative Research* (5th ed, 2011) Figure 8.2.

¹²⁷ See Uwe Flick, *An Introduction to Qualitative Research* (4th ed, 2009) 319.

dysfunctionality of legal enforcement, the role of gatekeepers in practice, the behaviour and expectations of minority shareholders, the powers and responsibilities of market authorities, and, legal transplants and their efficiency. Finally, the author extracted the statements from each interview and categorised them by identified themes.

One may argue that the themes found during the coding process were predictable as the interview data followed the guidelines of the interview schedule which, in turn, was based on the issues raised in the literature. The researcher, however, found that coding did not construct the results of the field work. The interviewees with different backgrounds reflected different opinions on the same issues. Coding is the process of organising the empirical data. Once organised, it demonstrated both supporting and contradicting statements.¹²⁸ It also led to new concepts emerging, from and pointed out by the interviewees, which were not mentioned in the interview schedule. The researcher acknowledged the character and influence of this data analysis method and, therefore while coding, the researcher did not limit herself only to the themes or the interview schedule but considered other ideas which emerged and which were useful for the thesis.

The analysis of the data collected was based on the research questions for this thesis. The information provided by the interviewees was considered in the context of each of those questions. It was compared with the theoretical concepts of minority shareholders' protection and possible alternative legal frameworks for their protection in the Thai regulatory framework. The interviewees' various viewpoints were used to find communal understandings and consensus on Thai business culture and legal protection for minority shareholders in Thailand. The data obtained from literature and media reviews, as well as the perspectives of experienced and informed participants, provides an understanding of existing law and regulatory practices and the suggestions for possible legal reform in Thailand. The same materials were triangulated to establish an opinion on contentious or disputed issues. The statements made by the interviewees were used to evaluate theoretical propositions throughout the thesis. Some portions of the interviewees' statements are cited to illustrate particular ideas or themes.

¹²⁸ As pointed out by Basit, '[r]esearchers have discussed coding in the context of data reduction, condensation, distillation, grouping and classification'. Basit, above n 121, 152.

1.3.5 Limitations of the research methodology

The research was designed to give a better understanding of minority shareholders' protection in Thailand. The qualitative approach was selected to facilitate in-depth exploration. The interviews were taken to gain experience through the viewpoints of related people. Although this research methodology is of benefit for the research, there are some issues to be aware of. As indicated the statements given by the interviewees are solely their opinions. The participants' attitudes and feelings cannot be easily assessed. In addition, there are several factors that may affect the results of the interviews, including motivation, emotion and the communicative ability of the participants. Furthermore, some participants may not point out some sensitive issues. To ensure that these concerns are managed a good understanding on the issue of confidentiality is required. Before the interviews were conducted, the researcher had informed the participants of the confidentiality of the information provided. The names and organisations of the participants are not disclosed in the research so that they remain anonymous. The statements or comments are also not published in a way that the participants could be identified.

The interviews fundamentally aimed to collect and analyse the personal appraisals and thoughts of the interviewees on minority shareholders' protection in Thailand. Although the professionals were selected on the basis of, and assumed to be representative of their occupational groups, the thesis makes no assumptions on the generalisations of the findings to a particular group. Besides, given the limitation of time, only a relatively small number of interviews were conducted. Individuals may provide the experiences they gain from working for their organisations but they cannot represent their organisations or all members of such organisations. The findings from these interviewees therefore reveal only the views of individuals regarding the system in which they work and are used together with documentary sources.

In addition, some literature used in the thesis was in Thai. The interviews were also conducted in Thai. Translation was therefore involved. As Regmin *et al* noted, translation was a process of converting field texts to research texts through making

decisions at different stages to obtain equivalent meanings and interpretations.¹²⁹ The translation process is therefore vital as it affects the validity of the work.¹³⁰ To maintain the accuracy of the text of the literature and interviewees' views and perspectives, the translation was done carefully with great caution.¹³¹

1.4 Outline of the thesis

The thesis comprises nine chapters. The first chapter introduces the background of the research, the research questions, and the research methodologies. The second chapter begins with a discussion of the concept of minority shareholders' protection, such as the concept of control and the definition of minority shareholders. The development of minority shareholders' protection in the US and German contexts is discussed. The study further examines the corporate structure and how minority shareholders are protected within East Asian contexts. The third chapter presents a fundamental understanding of the Thai legal framework on minority shareholders' protection. It provides some background on the development of Thai company law and the Stock Exchange of Thailand. It also examines how the reform of minority shareholders' protection has developed in Thailand. The significant details of the Thai corporate and securities laws on minority shareholders' protection are summarised.

The following chapters seek to prove the researcher's thesis that, even in the modern corporate sector in a developing economy with its characteristically dualistic structure, law reform through borrowing is problematic and that its success cannot be ensured unless proper adjustments are made to fit legal transplants into local conditions. In the fourth to the seventh chapters, the thesis moves to a discussion of how Thai laws protect minority shareholders by comparison with US and German laws. The fourth chapter discusses how minority shareholders can participate in significant decision-making and can exercise their rights properly and effectively. It surveys the legal framework governing shareholders' rights in the US, Germany, and Thailand in two categories:

¹²⁹ Krishna Regmi et al, 'Understanding the Processes of Translation and Transliteration in Qualitative Research' (2010) 9(1) *International Journal of Qualitative Methods* 16,18

¹³⁰ Philip J Larkin et al, 'Multilingual Translation Issues in Qualitative Research: Reflections on a Metaphorical Process' (2007) 17(4) *Qualitative Health Research* 468, 468.

¹³¹ Regmin et al, above n 129, 19.

management rights and proprietary rights. The fifth chapter reviews the laws and legal practices regarding the powers and duties of the board of directors in the three jurisdictions. This extends to a discussion of the liability of controlling shareholders in the US, German, and Thai contexts. The sixth chapter focuses on specific issues concerning mergers, takeovers, and related party transactions. The legal procedures that companies must follow to protect the interests of minority shareholders is also discussed. The seventh chapter outlines how the laws in the US, German, and Thai jurisdictions provide remedies for minority shareholders whose rights are injured. It also examines the roles of securities regulatory authorities in each jurisdiction.

As one of the research questions is the possible adoption of US and German law into the Thai legal system, the eighth chapter addresses the issues relating to legal transplants in Thai company law and their success and failure, and the future of such transplants. The ninth chapter contains the conclusions to the research questions, limitations on the answers, and implications for further research.

Chapter 2

The Nature of Minority Shareholders' Protection

- 2.1 Introduction
- 2.2 Conceptualising minority shareholders
 - 2.2.1 The concept of “control”
 - 2.2.2 Controlling and minority shareholders
- 2.3 The development of minority shareholders' protection in the United States
 - 2.3.1 Agency problems
 - 2.3.2 Controlling agency problems
 - 2.3.3 Regulatory mechanisms
- 2.4 Minority shareholders' protection under the German model
 - 2.4.1 The two-tier board system
 - 2.4.2 Co-determination
 - 2.4.3 The role of German banks
- 2.5 The concept of minority shareholders' protection in the East Asian context
 - 2.5.1 Ownership structure of East Asian corporations
 - 2.5.2 The effect of concentrated-ownership structure
 - 2.5.3 The application of Western corporate governance models
- 2.6 Conclusion

2.1 Introduction

This chapter reviews the literature on the concept of minority shareholders' protection. It firstly seeks to define “minority shareholder”. Then it outlines the development of the protection for minority shareholders in the United States and Germany. It also considers the concept in the context of East Asian countries¹ and points to the need to study minority shareholders' protection in this specific circumstance.

2.2 Conceptualising minority shareholders

The concept of minority shareholders needs to be understood in the context of other concepts, particularly the ownership structure of companies and the concept of control.

¹ Following the work of Claessens *et al*, East Asian countries consist of Hong Kong, Indonesia, Japan, South Korea, Malaysia, the Philippines, Singapore, Taiwan, and Thailand. Stijn Claessens, Simeon Djankov and Larry HP Lang, 'The Separation of Ownership and Control in East Asian Corporations' (2000) 58 *Journal of Financial Economics* 81.

Minority shareholders may be best understood in terms of what they are not, majority shareholders.

2.2.1 The concept of “control”

One of the most important questions regarding minority shareholders’ protection in listed companies is which shareholders should be classified as “minority shareholders”. In widely diffused corporations where no control exists, it may be the case that all shareholders are minority shareholders. In some companies, however, a group of minority shareholders may be able to control the company if they can collect sufficient proxies to produce a majority vote at a shareholders’ meeting – this collaboration is known as “minority control”.² Without minority control, the control of the company will be shifted into the hands of management. In concentrated ownership corporations, on the contrary, the line drawn between majority and minority shareholders becomes clearer as there are shareholders holding sufficient voting shares to dominate shareholders’ meetings.

Fama and Jensen placed the concept of control of a firm in the context of the corporate decision-making process consisting of four steps – initiation, ratification, implementation, and monitoring.³ They referred to the initiation and the implementation of decisions as ‘decision management’ and to the ratification and the monitoring of decisions as ‘decision control’.⁴ The power to initiate and implement a decision is in the managers’ hands, while the power to ratify and monitor a decision is in the shareholders’ hands.⁵ According to Fama and Jensen, control refers to the power of an individual or a group who could effectively control all the decision-making processes – initiation, ratification, implementation, and monitoring – within the firm. As the

² Adolf A Berle Jr and Gardiner C Means, *The Modern Corporation and Private Property* (1933) 79–84.

³ Eugene F Fama and Michael Jensen, 'Separation of Ownership and Control' (1983) 26 *Journal of Law and Economics* 301, 303.

⁴ Ibid 303–4.

⁵ Ibid 304.

direction of the firm is decided by the board of directors in particular the control of the firm is the ability to select the board of directors.⁶

The earlier studies defined the power over a corporation by considering whether the firm was controlled by shareholders or management. The criterion used was ownership percentage. Berle and Means suggested in the early 1930s that modern large corporations in the US were owned by a large number of minority shareholders.⁷ As the shares in publicly-listed companies were widely diffused, they drew a line between minority shareholders and management control 'roughly at 20 per cent' of voting stocks.⁸ La Porta *et al* expanded on their work to cover the corporate ownership of firms around the world⁹ and defined controlling shareholders as those who directly and indirectly hold over 20 per cent of voting rights in the firm.¹⁰

Cubbin and Leech disagreed with the use of a shareholding percentage to define the meaning of control.¹¹ They raised two important dimensions of the separation of ownership and control: the location of control and the degree of control.¹² Regarding location, control could either be inside or outside the management.¹³ External control was further divided between large individual shareholders and institutional investors.¹⁴ The degree of control is dependent on the location of control. The internal controllers are expected to have a higher degree of control than other shareholders outside the

⁶ Berle and Means extended the meaning of control to the case of that of an individual or a group who had control through dictating to the management, such as a seriously indebted corporation operating under a bank policy. See Berle and Means, above n 2, 69–70.

⁷ Ibid 3.

⁸ Ibid 93.

⁹ They concluded that there are five types of ultimate owners: (i) a family or an individual; (ii) a state; (iii) a widely-held financial institution, such as a bank or an insurance company; (iv) a widely-held corporation; and (v) miscellaneous, such as a corporate, a voting trust, or a group with *no single controlling investors*. Rafael La Porta, Florencio Lopez-de-Silanes and Andrei Shleifer, 'Corporate Ownership Around the World' (1999) 54(2) *The Journal of Finance* 471, 476.

¹⁰ Ibid 476–7; Claessens *et al* had also applied a similar cut-off level to examine firms in East Asian countries. See Claessens, Djankov and Lang, above n 1.

¹¹ John Cubbin and Dennis Leech, 'The Effect of Shareholding Dispersion on the Degree of Control in British Companies: Theory and Measurement' (1983) 93 *The Economic Journal* 351; Helen Short, 'Ownership, Control, Financial Structure and the Performance of Firms' (1994) 8(3) *Journal of Economic Surveys* 203, 216.

¹² Cubbin and Leech, above n 11, 354.

¹³ Ibid.

¹⁴ Ibid 354–5.

internal management.¹⁵ The degree of control is measured by the voting power exercised by a group of controlling shareholders.¹⁶ Cubbin and Leech defined a controlling shareholder as the one who has a specified high degree of control and is able to control the exercise of the discretion of the firm.¹⁷ The sizes of controlling shareholdings therefore vary according to the shareholding dispersion within firms.¹⁸

As these studies indicated, there is no consensus on the level of ownership that effectively controls a firm.¹⁹ However, from the relevant studies, two criteria may be used to define the concept of “control”: (i) a specific threshold of voting shares; and, (ii) a substantial degree of control or influence over the management. Due to variations in the dispersion of shareholders, the cut-off level is generally based on country specific conditions. For instance, in a country where ownership of listed companies are widely dispersed, a shareholder who owns at least 10 per cent of voting stocks may be able to control the company. On the contrary, in other countries where ownership of listed companies is concentrated, a shareholder may have to hold more than 30 or 40 per cent of voting stocks to control the firm. Also, defining the meaning of “control” often involves references to the ability to control the corporation’s affairs. The research therefore follows Cubbin and Leech’s analysis, suggesting that the ability to control a firm may be in the form of the power to appoint the directors or at least half of the directors, or to have an influence over corporate strategy decisions.²⁰

2.2.2 Controlling and minority shareholders

Due to these differences over the meaning of “control”, the concepts of “control”, “controlling shareholders” and “minority shareholders” in the three jurisdictions need to be considered to understand the concept of “minority shareholders”.

¹⁵ Ibid 355.

¹⁶ Ibid.

¹⁷ Ibid 367.

¹⁸ Ibid.

¹⁹ Short had studied 26 empirical works regarding the definition of control and found inconsistent results. The study explains that the reason underlying this is the different interpretation of “control” applied in different studies. Short, above n 11, 216, Table 1.

²⁰ See also Fama and Jensen, above n 3.

In the US, the concept of control is found in both securities and corporate laws. At the level of federal statutes, the term “control” means the direct or indirect possession of the power to direct or cause the direction of the management and policies of a company, whether through the ownership of voting securities, the contract, or otherwise.²¹ Under the Delaware General Corporations Law, the fundamental idea of control is similar to that in federal law. The state law goes further in stipulating that a person who owns at least 20 per cent of voting stocks is assumed to have a control over such an entity.²²

In Germany, the definition of the term “control” is found in the *Wertpapiererwerbs- und Übernahmegesetz* of 2001 [Securities Acquisition and Takeover Act]. The law states that “control” is the holding of at least 30 per cent of the voting rights in the target company.²³ The *Aktiengesetz* of 2009 [Stock Corporation Act] also defines the meaning of “control” under provisions regarding affiliated enterprises.²⁴ The Act uses the ownership of the majority of the shares as the threshold in defining whether an enterprise is held by another enterprise.²⁵

In Thailand, the concept of “control” is found in the listing rules. The rules state that “controlling shareholders” are those who have significant influence over a company’s policy processes, management, or operations.²⁶ They also define a controlling shareholder as a shareholder who directly or indirectly owns at least 25 per cent of a company’s voting rights.²⁷ The rule further defines the term “major shareholder” as a

²¹ See Securities Act of 1933 Rule 405; Securities and Exchange Act of 1934 Rule 12b-2.

²² Delaware General Corporation Law §203(c)(4).

²³ *Wertpapiererwerbs- und Übernahmegesetz* of 2001 [Securities Acquisition and Takeover Act] (Germany) § 29.

²⁴ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) §§ 15–22.

²⁵ *Ibid* § 16.

²⁶ SET Listing Rules Bor.Jor./Ror.01-11 Attachment 1.

²⁷ *Ibid*. The 25 per cent threshold is in accordance with the study of Wiwattanakantang which showed that, on average, the largest shareholder alone accounts for 24.65 per cent of a company’s shares. Yupana Wiwattanakantang, 'The Equity Ownership Structure of Thai Firms' (Working Paper No 2001-8, Hitotsubashi University, Center of Economic Institutions, 2000) 7; See also Yupana Wiwattanakantang, 'An Empirical Study on the Determinants of the Capital Structure of Thai Firms' (1999) 7 *Pacific-Basin Financial Journal* 371, 377. Besides, under Thai law, the 25 per cent ownership threshold gives a shareholder sufficient power to influence a company’s decision. See eg Public Company Act B.E. 2535 (1992) (Thailand) ss 31, 54/1, 136, 139, 146, 154.

person who, directly and indirectly, holds more than 10 per cent of total voting shares of the company or its subsidiary.²⁸

In the three jurisdictions, the definitions of “control” or “controlling shareholders” are used in corporate and securities laws. A specific threshold of voting shares is not a prerequisite to securing of corporate control. As suggested by Cubbin and Leech, the shareholding percentage to be divided between controlling and minority shareholders is not used in considering who is a majority shareholder and who, therefore, is considered to be a minority shareholder, but mainly relies on whether a shareholder has a form of control over a company.

2.3 The development of minority shareholders’ protection in the United States

To provide a more complete understanding of the concept of minority shareholders’ protection, it is considered in two models: common and civil law. As mentioned in the first chapter, US law is used to reflect on the mechanisms applied in common law jurisdictions and German law to represent those applied in civil law models.

Under the pressure of globalisation and international trade, including the trade in financial capital, similarly to other developing countries, Thailand has been influenced by Anglo-American commercial law. A number of legal concepts from US law have been incorporated into the Thai legal system. Reflecting on the development of minority shareholders’ protection in the US assists in understanding how the adopted concepts have been developed in Thai law; and in considering whether the adopted mechanisms which have been long developed in US business and legal practices, can provide better protection for minority shareholders in Thailand.

2.3.1 Agency problems

Berle and Means claimed that, in the context of the structure of large listed corporations, the management function had shifted away from entrepreneurial owners to

²⁸ SET Listing Rules Bor.Jor.46/55.

administrators, or managers.²⁹ They found that the size of US firms had significantly increased with massive numbers of individual stockholders.³⁰ Each of the shareholders in large corporations was a minority shareholder and thus had no control over these corporations.³¹ The decision-making control had, consequently, transferred into the hands of professional managers.³² The shareholders might have their opinions considered at shareholder meetings; however, this did not imply that shareholders had control over the company.³³ The shareholders' interests had become limited to the returns on the money they had invested, in the form of dividends, and the increase of their shares' value.³⁴

Jensen and Meckling, following Berle and Means, developed the agency theory to explain the relationship between shareholders and managers. Through a contract, shareholders (principals) hire managers (agents) to act on the shareholders' behalf.³⁵ The risk is that the actions of the agents may not be in the interests of the principals. Jensen and Meckling assumed that agents tended to promote their own self-interest.³⁶ The principals expect the agents to maximise their profit but, on the contrary, the agents' concern is with their own self-interest rather than the interests of the principals. To minimise such risks, the principals must seek to reconcile the divergence between the principals and agents. This reconciliation incurs costs to the principals. For instance, to ensure the appropriateness of the agents' activities, principals must constantly monitor the agents' activities and this monitoring incurs significant costs.

²⁹ Berle and Means, above n 2, 93–4 and Table XII.

³⁰ Ibid 3.

³¹ Ibid 117. Berle further claimed:

As of today, it is probably true that stockholders have saved (or have inherited past savings). But, as we have noted, these savings no longer are a major source of capital. At best, not over 2 or 3 per cent (often less) of new risk-capital actually entering industrial enterprise in each year is supplied from this resource.

See Adolf A Berle, 'The Impact of the Corporation on Classical Economic Theory' (1965) 79(1) *The Quarterly Journal of Economics* 25, 37–8.

³² Berle and Means, above n 2, 154.

³³ Ibid 138–141.

³⁴ Ibid 189.

³⁵ Michael Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 *Journal of Financial Economics* 305, 308.

³⁶ Ibid.

From the observations of Berle and Means, and those of Jensen and Meckling, the key problem is that the managers who initiate and implement decisions that affect the residual claimants in the company, the shareholders, do not bear any risks from the consequences of such a decision.³⁷ The control of the decision-making process is therefore necessary to ensure that the managers will not pursue their interests at the shareholders' expense.

2.3.2 Controlling agency problems

One of the mechanisms used to reduce agency problems is managerial ownership. As mentioned above, the key problem is that the benefits to managers may be different from those to shareholders. If the corporate insiders, managers or members of the board, have a direct interest in the company as shareholders, the divergence between the positions of residual claimants and agents may be minimised.³⁸ It is claimed that managerial shareholdings have a significant connection with corporate performance.³⁹ Different empirical studies have affirmed that changes in inside ownership have a positive impact on corporate value.⁴⁰ Fahlenbrach, for instance, found that 11 per cent of the largest US firms were headed by the chief executive officers (CEO) that founded the firm. These firms earned a significantly higher return than others.⁴¹ However, a number of scholars question whether managerial ownership could actually reduce the risk of conflict between managers and shareholders. Demsetz argued that the increase in firm value was not a direct result of managerial ownership as there were various

³⁷ Fama and Jensen, above n 3, 304; Eugene F Fama and Michael Jensen, 'Agency Problems and Residual Claims' (1983) 26 *Journal of Law and Economics* 327, 331. See also Benjamin Klein, 'Contracting Costs and Residual Claims: The Separation of Ownership and Control' (1983) 26(2) *Journal of Law and Economics* 367.

³⁸ John J McConnell and Henri Servaes, 'Additional Evidence on Equity Ownership and Corporate Value' (1990) 27 *Journal of Corporate Finance* 595, 610–1.

³⁹ Randall Morck, Andrei Shleifer and Robert W Vishny, 'Management Ownership and Market Valuation: An Empirical Analysis' (1988) 20 *Journal of Financial Economics* 293; Clifford G Holderness, Randall S Kroszner and Dennis P Sheehan, 'Were the Good Old Days That Good? Changes in Managerial Stock Ownership Since the Great Depression' (1999) 54(2) *The Journal of Finance* 435; Ronald C Anderson and David M Reeb, 'Founding-Family Ownership and Firm Performance: Evidence from the S&P 500' (2003) 58(3) *The Journal of Finance* 1301.

⁴⁰ McConnell and Servaes, above n 38; John J McConnell and Henri Servaes, 'Equity Ownership and the Two Faces of Debt' (1995) 39 *Journal of Financial Economics* 131; John J McConnell, Henri Servaes and Karl V Lins, 'Changes in Insider Ownership and Changes in the Market Value of the Firm' (2008) 14 *Journal of Corporate Finance* 92.

⁴¹ Rüdiger Fahlenbrach, 'Founder-CEOs, Investment Decisions, and Stock Market Performance' (2009) 44(2) *The Journal of Financial and Quantitative Analysis* 439.

relevant factors, especially competitive markets.⁴² Following Demsetz and Lehn,⁴³ Demsetz and Villalonga,⁴⁴ Seifert *et al*,⁴⁵ Himmelberg *et al*,⁴⁶ and Tong,⁴⁷ affirm that the level of insider share ownership does not directly increase firm performance.⁴⁸

In addition to insider ownership, monitoring by shareholders is another mechanism used to ensure that managers will employ their best efforts to prioritise the shareholders' interest. However, shareholders, especially minority ones, have little incentive to monitor management. Given the small fraction of shares they own, the cost of monitoring exceeds any gain they may receive. Consequently shareholders are likely to expect other shareholders to monitor the management and they will benefit from the monitoring without having to bear any cost. This is known as free-riding.⁴⁹

Huddart explained that only shareholders with a significant number of shares have an incentive to monitor managers, and that minority shareholders tend to delegate their monitoring duties to these larger shareholders.⁵⁰ These larger shareholders may be the founders of the corporation, institution investors, or other financial firms.⁵¹ Shleifer and Vishny also argued that firms with concentrated ownership have higher firm values than

⁴² Harold Demsetz, 'The Structure of Ownership and the Theory of the Firm' (1932) 26(2) *Journal of Law and Economics* 375, 379–80.

⁴³ Harold Demsetz and Kenneth Lehn, 'The Structure of Corporate Ownership: Causes and Consequences' (1985) 93(6) *Journal of Political Economy* 1155.

⁴⁴ Harold Demsetz and Belen Villalonga, 'Ownership Structure and Corporate Performance' (2001) 7(3) *Journal of Corporate Finance* 209.

⁴⁵ Bruce Seifert, Halit Gonenc and Jim Wright, 'The International Evidence on Performance and Equity Ownership by Insiders, Blockholders, and Institutions' (2005) 15 *Journal of Multinational Financial Management* 171.

⁴⁶ Charles Himmelberg, PR Glenn Hubbard and Darius Palia, 'Understanding the Determinants of Managerial Ownership and the Link between Ownership and Performance' (1999) 53 *Journal of Financial Economics* 353. See Xianming Zhou, 'Understanding the Determinants of Managerial Ownership and the Link between Ownership and Performance: Comment' (2001) 62 *Journal of Financial Economics* 559.

⁴⁷ Zhenxu Tong, 'Deviations from Optimal CEO Ownership and Firm Value' (2008) 32(11) *Journal of Banking & Finance* 2462.

⁴⁸ Holderness, Kroszner and Sheehan, above n 39. See also J R Davies, David Hillier and Patrick McColgan, 'Ownership Structure, Managerial Behavior and Corporate Value' (2005) 11 *Journal of Corporate Finance* 645.

⁴⁹ See Anat R Admati, Paul Pfleiderer and Josef Zechner, 'Large Shareholder Activism, Risk Sharing, and Financial Market Equilibrium' (1994) 102(6) *The Journal of Political Economy* 1097.

⁵⁰ Steven Huddart, 'The Effect of a Large Shareholder on Corporate Value' (1993) 39(11) *Management Science* 1407, 1417–8.

⁵¹ Andrei Shleifer and Robert W Vishny, 'Large Shareholders and Corporate Control' (1986) 94(3) *The Journal of Political Economy* 461, 462.

those with diffused ownership.⁵² Likewise, having examined the relationship between founding-family ownership and firm performance, Anderson and Reeb found that family firms performed better than non-family ones.⁵³ This was because large shareholders not only monitored the management but also, in some cases, intervened in managements' decision.⁵⁴ Some prominent investors, such as Warren Buffet, the LENS Fund, and Bennet LeBow, generally purchased blocks of shares in companies with high capacity but low performance.⁵⁵ They then intervened in management to improve firm performance.⁵⁶ Pound also found that large institutional investors took part in reforming corporate governance in a firm.⁵⁷ Due to their significant shareholdings, institutional investors could also exert pressure for specific changes in a company that they believe will lead to better governance.⁵⁸ Despite this literature, other scholars argue that the benefits of increased oversight of institutional investors have not been proven.⁵⁹ Jones *et al* claimed that there is a positive relationship between institutional ownership and corporate value but when a corporation has concentrated ownership by institutional investors, the relationship becomes negative.⁶⁰ Smith examined the performance of the firms targeted by CalPERS and found that the structure of such firms had changed and consequently the firms' values had increased. Nonetheless, the operating performance of the firms was not significantly improved.⁶¹

⁵² Ibid 461. See also Michael J Barclay, Clifford G Holderness and Jeffrey Pontiff, 'Private Benefits from Block Ownership and Discounts on Closed-end Funds' (1993) 33(3) *Journal of Financial Economics* 263, 263.

⁵³ Anderson and Reeb, above n 39, 1303; see also Jennifer E Bethel, Julia Porter Liebeskind and Tim Opler, 'Block Share Purchases and Corporate Performance' (1998) 53(2) *The Journal of Finance* 605, 605–6; Dechun Wang, 'Founding Family Ownership and Earning Equity' (2006) 44(3) *Journal of Accounting Research* 619.

⁵⁴ See Belén Villalonga and Raphael Amit, 'Family Control of Firms and Industries' (2010) 39(3) *Financial Management* 863.

⁵⁵ Thomas H Noe, 'Investor Activism and Financial Market Structure' (2002) 15(1) *The Review of Financial Studies* 289, 290.

⁵⁶ Ibid.

⁵⁷ John Pound, 'Raiders, Targets, and Politics: The History and Future of American Corporate Control' (1992) 5(3) *Journal of Applied Corporate Finance* 6, 13.

⁵⁸ Ibid 17.

⁵⁹ See, eg, Bernard S Black, 'Institutional Investors and Corporate Governance: The Case for Institutional Voice' (1992) 5 *Journal of Applied Corporate Finance* 19, 20.

⁶⁰ Steven L Jones, Darrell Lee and James G Tompkins, 'Corporate Value and Ownership Structure in the Post-Takeover Period: What Role Do Institutional Investors Play?' (1997) 18 *Managerial and Decision Economics* 627, 640.

⁶¹ Michael P Smith, 'Shareholder Activism by Institutional Investors: Evidence from CalPERS' (1996) 51(1) *The Journal of Finance* 227, 251. For a study on the performance of family firms, see Danny Miller *et al*, 'Are Family Firms Really Superior Performers?' (2007) 13 *Journal of Corporate Finance* 829.

Apart from oversight by shareholders, another mechanism for monitoring the management is the board of directors. The board has the power to evaluate the performance of the CEO, provide recommendations, and ensure that the shareholders' interests are well protected.⁶² Some scholars claim that having outsiders appointed to the board of directors improves the effectiveness of the board.⁶³ This mechanism is a requirement which companies listed on the New York Stock Exchange (NYSE) must follow.⁶⁴ From their investigation of 142 NYSE trading companies, Hermalin and Weisbach found that the boards were responsible for poor performance and some insiders were forced to relinquish their positions.⁶⁵ To fill these vacant positions, outsiders were appointed with the expectation of better monitoring of management.⁶⁶ Schellenger *et al* studied the relationship between board composition and firm performance and reported that having outside directors on the boards has a positive effect.⁶⁷ Nevertheless, other researchers disagree. Baysinger and Butler explored such a relationship and found that the firms with a high proportion of independent directors perform above firms with none. However, it is unclear that such a difference was the consequence of actions of outside shareholders.⁶⁸ Other writers argued that outside directors are ineffective.⁶⁹ Brundney claimed that outsiders are not in a position to

⁶² Shaker A Zahra and John A II Pearce, 'Boards of Directors and Corporate Financial Performance: A Review and Integrative Model' (1989) 15(2) *Journal of Management* 291, 292. For details regarding the perspectives on boards of directors, see Table 1 in this article.

⁶³ Ibid 305–7; Mark S Mizruchi, 'Who Controls Whom? An Examination of the Relation between Management and Boards of Directors in Large American Corporations' (1983) 8(3) *The Academy of Management Review* 426, 426–7; Victor H Palmieri, 'Corporate Responsibility and the Competent Board' (1979) 57(3) *Harvard Business Review* 46, 47.

⁶⁴ The discussion on this issue is in Chapter 4.

⁶⁵ Benjamin E Hermalin and Michael S Weisbach, 'The Determinants of Board Composition' (1988) 19(4) *The RAND Journal of Economics* 589, 604–5.

⁶⁶ Ibid 605.

⁶⁷ Michael H Schellenger, David Wood and Ahmad Tashakori, 'Board of Director Composition, Shareholder Wealth, and Dividend Policy' (1989) 15(3) *Journal of Management* 457, 465–6. See also Michael L McDonald, James D Westphal and Melissa E Graebner, 'What Do They Know? The Effects of Outside Director Acquisition Experience on Firm Acquisition Performance' (2008) 29 *Strategic Management Journal* 1155.

⁶⁸ Barry Baysinger and Henry N Butler, 'Corporate Governance and the Board of Directors: Performance Effects of Changes in Board Composition' (1985) 1(1) *Journal of Law, Economics, & Organization* 101, 121. See also Scott W Barnhart, M Wayne Marr and Stuart Rosenstein, 'Firm Performance and Board Composition: Some New Evidence' (1994) 15(4) *Managerial and Decision Economics* 329, 338; Chenchuramaiah T Bathala and Ramesh P Rao, 'The Determinants of Board Composition: An Agency Theory Perspective' (1995) 16(1) *Managerial and Decision Economics* 59, 67.

⁶⁹ Paul Mallette and Raymond L Hogler, 'Board Composition, Stock Ownership and the Exemption of Directors from Liability' (1995) 21(5) *Journal of management* 861; Jerilyn W Coles and William S Hesterly, 'Independence of the Chairman and Board Composition: Firm Choices and Shareholder Value'

effectively monitor the management.⁷⁰ To do this requires significant time and energy.⁷¹ They must be knowledgeable about the company's business affairs. They would also be under pressure from board members and shareholders. Due to heavy workloads, outside directors may not be able to monitor the management effectively. The purpose of having outsiders on the board is to ensure their independence. However, the absence of interests in the company, outsiders have no economic interests or the incentive to act in the best interest of its shareholders.⁷²

These four mechanisms – managerial ownership, institutional shareholdings, shareholding by blockholders, and outsiders on the board of directors – are internal to corporations. They work together to ensure that agency costs are minimised. In addition, there are external mechanisms – the labour market and the market for corporate control.⁷³ Fama suggested that the managers are controlled by the markets for their services both inside and outside the firm.⁷⁴ The top-level managers are monitored by managers at the lower level and by managers at the same level.⁷⁵ Competition among the top managers for the CEO position would ensure that they would make appropriate decisions. The performance of managers is evaluated not only within but also outside the firm.⁷⁶ Outside managers, with a record of better performance in the external labour market, may be appointed to replace ineffective managers.⁷⁷ Fee and Hadlock studied the correlation between firm performance and managers' promotion opportunities and

(2000) 26(2) *Journal of management* 195; Yuval Deutsch, 'The Impact of Board Composition on Firms' Critical Decisions: A Meta-Analytic Review' (2005) 31(3) *Journal of management* 424.

⁷⁰ See Victor Brudney, 'The Independent Director – Heavenly City or Potemkin Villages?' (1982) 95 *Harvard Law Review* 597.

⁷¹ Ibid 633.

⁷² Ibid 634.

⁷³ Grossman and Hart also suggested the other mechanism: the possibility of bankruptcy. See Sanford J Grossman and Oliver D Hart, 'Corporate Financial Structure and Managerial Incentives' in John McCall (ed), *The Economics of Information and Uncertainty* (1982) 108.

⁷⁴ Eugene F Fama, 'Agency Problems and the Theory of the Firm' (1980) 88(2) *The Journal of Political Economy* 288, 289; Cf Bengt Holmström, 'Managerial Incentive Problems: A Dynamic Perspective' (1999) 66(1) *The Review of Economic Studies* 169.

⁷⁵ Fama, above n 74, 289.

⁷⁶ Ján Zábajník, 'On the Efficiency of Markets for Managers' (2001) 18(3) *Economic Theory* 701, 706.

⁷⁷ C Edward Fee and Charles J Hadlock, 'Management Turnover and Product Market Competition: Empirical Evidence from the US Newspaper Industry' (2000) 73(2) *The Journal of Business* 205. Fee and Hadlock found the relationship between competition and management turnover.

suggested that high-performance managers have opportunities in the market to get a CEO position with another corporate employer.⁷⁸

The other mechanism working in close collaboration with the external labour market for managers is the market for corporate control.⁷⁹ That concept was developed initially by Manne, following Berle and Means. He suggested that:

A fundamental premise underlying [concept] is the existence of a high positive correlation between corporate managerial efficiency and the market price of shares of that company.⁸⁰

After evaluating the firm's potential and finding that the poor performance is a direct outcome of poor management, outsiders may take over⁸¹ the corporation as they believe that, with more effective management, the firm will generate a greater return.⁸² Shareholders can also signal to outsiders if a significant number constantly sell their shares.⁸³ Shleifer and Vishny further clarified the role of takeovers for correcting the failure of internal control.⁸⁴ Due to the imperfections in monitoring management for failure or inefficiencies, a hostile takeover is the greatest disciplining device.⁸⁵ This suggests that the market for corporate control benefits not only the shareholders of acquired firms but drives efficiencies in the corporate sector as a whole.⁸⁶ The market

⁷⁸ C Edward Fee and Charles J Hadlock, 'Raids, Rewards, and Reputations in the Market for Managerial Talent' (2003) 16(4) *The Review of Financial Studies* 1315, 1316, 1352.

⁷⁹ Michael Jensen, 'Takeovers: Their Causes and Consequences' (1988) 2(1) *The Journal of Economic Perspectives* 21, 23.

⁸⁰ Henry G Manne, 'Mergers and the Market for Corporate Control' (1965) 73(2) *The Journal of Political Economy* 110, 112.

⁸¹ Halpern explained the takeover process:

Mergers occur when an acquiring firm and a target firm(s) agree to combine under legal procedures established in the states in which the merger participants are incorporated. A tender offer is an offer to purchase a proportion of the outstanding shares of the target firm at specified terms on or before a specified date. Those shareholders not tendering their shares retain an ownership interest in the firm. The term "acquisition" is used in a generic sense to refer to any takeover.

Paul Halpern, 'Corporate Acquisitions: A Theory of Special Cases? A Review of Event Studies Applied to Acquisitions' (1983) 38(2) *The Journal of Finance* 297, 297.

⁸² Manne, above n 80, 113.

⁸³ See Edward Jay Epstein, *Who Owns the Corporation? Management vs. Shareholders* (Priority Press Publication, 1986) 24–5.

⁸⁴ Andrei Shleifer and Robert W Vishny, 'Value Maximization and the Acquisition Process' (1988) 2(1) *The Journal of Economic Perspectives* 7, 8–11.

⁸⁵ Ibid 11. See also Ronald W Masulis, Cong Wang and Fei Xie, 'Corporate Governance and Acquirer Returns' (2007) 62(4) *The Journal of Finance* 1851, 1884.

⁸⁶ Jensen, above n 79, 45; Paul Halpern, 'Corporate Acquisitions: A Theory of Special Cases? A Review of Event Studies Applied to Acquisitions' (1983) 38(2) *The Journal of Finance* 297, 314; Gregg A Jarrell, James A Brickley and Jeffry M Netter, 'The Market for Corporate Control: The Empirical Evidence Since

for corporate products and services competition, as Hart explained, also may ‘reduce the managerial slack’.⁸⁷ As it is difficult to evaluate managerial effort, owners observe the outcomes of managers’ decisions through firm performance. When the costs of the firm and that of other firms in a similar industry are similar, the managers must fulfil profit targets and consequently managerial slack will be diminished.⁸⁸

Some scholars question the efficiency of these market mechanisms. Hogarty evaluated the profitability of merger activities and concluded that mergers are not profitable.⁸⁹ Scherer observed tender offer takeovers and found that the takeover schemes do not improve the long-term operating profitability of the target companies.⁹⁰ Similarly, Laamanen and Keil studied the most active acquirers in seven industry sectors and suggested that the direct effect of acquisitions is negative.⁹¹

2.3.3 Regulatory mechanisms

Based on agency theory, the above-mentioned mechanisms have developed under the assumption that firms are under the control of managers, and to ensure that managers are more concerned with the shareholders’ interests. In addition, US corporate law plays a supplementary role in protecting minority shareholders’ interests. The assumptions resulting from Berle and Means are that shareholders own small fractions of a company’ shares and that they therefore have neither the power nor incentives to monitor the management. This is reflected in the US Congress enacting the Securities Act of 1933 (“Securities Act”) and the Securities Exchange Act of 1934 (“Exchange Act”) to

1980’ (1988) 2(1) *The Journal of Economic Perspectives* 49, 66; James P Walsh and James K Seward, ‘On the Efficiency of Internal and External Corporate Control Mechanisms’ (1990) 15(3) *The Academy of Management Review* 421, 435.

⁸⁷ Oliver D Hart, ‘The Market Mechanism as an Incentive Scheme’ (1983) 14(2) *The Bell Journal of Economics* 366, 366. Grabowski *et al* also found that the threat of takeovers improves the efficiency of firms. Richard Grabowski, Ike Mathur and Nanda Rangan, ‘The Role of Takeovers in Increasing Efficiency’ (1995) 16(3) *Managerial and Decision Economics* 211.

⁸⁸ *Ibid.*

⁸⁹ Thomas F Hogarty, ‘Profits from Merger: The Evidence of Fifty Years’ (1969) 44 *St. John’s Law Review* 378, 389.

⁹⁰ FM Scherer, ‘Corporate Takeovers: The Efficiency Arguments’ (1988) 2(1) *The Journal of Economic Perspectives* 69, 80.

⁹¹ Tomi Laamanen and Thomas Keil, ‘Research Notes and Commentaries: Performance of Serial Acquirers: Toward an Acquisition Program Perspective’ (2008) 29 *Strategic Management Journal* 663, 670.

‘provide better and more information to shareholders for effective control over management’.⁹²

Regulatory mechanisms providing some protection to minority shareholders include the rules on proxy solicitation and shareholder proposals. The detailed discussion of these is in Chapter 4. Rules on proxy solicitation first appeared in the Exchange Act to ensure that the shareholders were fully informed of all matters on which they were asked to vote at shareholders’ meetings.⁹³ Any materials used to solicit shareholders’ votes for the election of directors and the approval of other corporate actions must comply with the rules as the Securities and Exchange Commission (“SEC”) prescribed.⁹⁴ Proxy solicitation was further addressed during the 1980s when hostile takeover transactions dominated the stock market.⁹⁵ Takeover entrepreneurs tended to acquire shares at a very low price then sell off the acquired company’s assets to make a profit rather than deploy them in an ongoing business strategy. The boards of target companies also developed some takeover defences, such as the poison pill or golden parachute. Acquiring companies responded to takeover defences by attempting to acquire sufficient votes from shareholders to install new management. Together with takeover activities, the other factor driving the growth of shareholder rights activism was the emergence of institutional shareholders. The institutional ownership of the US equity market continually increased from 33.1 per cent in 1980 to 53.3 per cent in 1990.⁹⁶ They generally voted in favour of takeover bids and against the board. They also heavily pushed proxy reform to strengthen their voting power and limit the managements’ power. CalPERS was the first institution proposing proxy reform to the SEC in 1989. Later the United Shareholders Association also called for reform. In 1991 the SEC announced a project to reform the federal proxy system and the amendment of the proxy

⁹² Carol Goforth, 'Proxy Reform as a Means of Increasing Shareholder Participation in Corporate Governance: Too Little, but not Too Late' (1993–1994) 43 *American University Law Review* 379, 386.

⁹³ Jeffrey Bauman, Elliott Weiss and Alan Palmiter, *Corporations Law and Policy: Materials and Problems* (5th ed, 2003) 480–1.

⁹⁴ Securities Exchange Act of 1934 § 14(a).

⁹⁵ See Nell Minow, 'Proxy Reform: The Case for Increased Shareholder Communication' (1991–1992) 17 *Journal of Corporation Law* 149.

⁹⁶ Carolyn K Brancato, 'Institutional Investors and Capital Markets: 1991 Update' (Center for Law and Economic Studies, Columbia University School of Law, 1991) 8.

solicitation regulations took effect in 1992.⁹⁷ In addition to proxy solicitation, the Exchange Act introduced the idea of shareholder proposals to facilitate shareholders' control over management and participation in corporate decision-making.⁹⁸ This mechanism allows qualified shareholders to place their proposals in the managements' material sent to all shareholders.⁹⁹

Another mechanism available to minority shareholders to control the management is litigation which be discussed further in Chapter 7. Shareholders can bring a legal action on behalf of a company – known as a derivative action – against directors for misconduct. As any amount recovered is returned to the company, the plaintiff shareholders are entitled to an indemnity for litigation costs from the company. Derivative actions serve a significant role in monitoring and deterring managerial malfeasance. The other type of shareholder litigation that is frequently used is a class action. This action allows a group of shareholders to aggregate their claims against a corporation in a cost effective way. Without this mechanism, each shareholder is unlikely to bring a legal action, as the stake in the company is too small to justify the time, effort, and the expense of litigation.

Together with private enforcement, the market supervisor also plays an important role to ensure regulatory compliance, maintain market stability and to improve investor protection. The SEC was founded by the Exchange Act after the Wall Street crash in 1929. Originally, the key roles of the SEC were to oversee stock trading and ensure compliance with securities laws. Since 1990 the role of the SEC has been significantly changed. The SEC was authorised to order disgorgement, forcing a defendant to give up the amount by which it was unjustly enriched. As a partial consequence of the collapse of Enron, the Congress enacted the Sarbanes-Oxley Act of 2002 extending the SEC's power to collect assets to reimburse injured investors. Recently, due to the global

⁹⁷ In June 1991, the SEC issued the first proxy reform proposal. The proposal had been largely criticised by representatives of both shareholders and managements. The deadline of comment was extended from early August to September 1991. The SEC finally decided to take the proposal back to reconsider it and issue a revised version. Minow, above n 95, 153–4.

⁹⁸ Daniel E Lazaroff, 'Promoting Corporate Democracy and Social Responsibility: The Need to Reform the Federal Proxy Rules on Shareholder Proposals' (1997–1998) 50 *Rutgers Law Review* 33, 34–6.

⁹⁹ Securities Exchange Act of 1934 Rule 14a-8.

financial crisis, the role of the SEC has been further readdressed. The detailed discussion of the present powers of the SEC is in Chapter 7.

The US model has been developed under the assumption that shareholders own only a small fraction of a company's shares and that they, therefore, have neither power nor incentive to monitor the management. In 1997, Shleifer and Vishny observed that, in most countries, firms are controlled by families and consequently the fundamental agency problem is the conflict between outside investors and controlling shareholders, rather than between outside investors and managers.¹⁰⁰ It is, therefore, questionable whether the mechanisms long developed in the US are applicable in other countries. Due to different corporate governance structures, mechanisms that work well in one country may not in other countries. This issue is discussed in Section 2.5.

2.4 Minority shareholders' protection under the German model

Although Anglo-American commercial law has had a significant influence on Thai law, the US and Thai legal systems belong to different legal families. The Thai legal system has been largely influenced by the German civil law system. The study of the German model of minority shareholders' protection is useful in the Thai context because, firstly, laws with similar legal heritages may be more easily adopted. Secondly, German legal principles and rules in themselves may provide an alternative approach for Thailand to take.

Unlike US listed corporations, shares of large German corporations are not widely held by a great number of small shareholders. Frank's and Mayer's study in 2001 of 171 large industrial listed companies found that 85 per cent of them were controlled by at least one large shareholder.¹⁰¹ German institutional investors did not have a significant

¹⁰⁰ Andrei Shleifer and Robert W Vishny, 'A Survey of Corporate Governance' (1997) 52(2) *The Journal of Finance* 737, 770.

¹⁰¹ Julian R Franks and Colin Mayer, 'Ownership and Control of German Corporations' (2001) 14(4) *Review of Financial Studies* 943, Table 1. See also Julian R Franks, Colin Mayer and Hannes F Wagner, 'The Origins of the German Corporation – Finance, Ownership and Control' (2006) 10(4) *Review of Finance* 537. Vistols also found that non-financial companies and founder/families still played the role as controlling shareholders. Sigurt Vitols, 'German Corporate Governance in Transition: Implications of

role as they accounted for only 14.7 per cent of the market.¹⁰² When the shares of companies sampled were owned by other corporations, Frank and Mayer further considered who the ultimate shareholders of such corporations were. They found the wide use of pyramid structures and cross-shareholdings. These financial patterns enabled a shareholder to have an indirect control over an ultimate company through other corporations. For instance, the study showed that family groups held 20.4 per cent of shares in German corporations; however, after tracking the ultimate shareholders of the control line, it concluded that the family shareholdings accounted for 33 per cent of ultimate shareholdings.¹⁰³ Other research in the late 1990s has estimated that around 96.96 per cent of German listed stock corporations were parts of a group known as *Konzerne*.¹⁰⁴ In the context where large shareholders have control over listed companies, how does the German model protect minority shareholders?

2.4.1 The two-tier board system

German corporate governance is recognised as an internal model because corporate control mainly exists inside corporations.¹⁰⁵ Unlike the US, there is almost no market for corporate control.¹⁰⁶ The German capital market is relatively shallow and small.¹⁰⁷ Initial public offerings have been rare.¹⁰⁸ Importantly, takeovers rarely happen because of the control by blockholders.¹⁰⁹ In the US, the structure of corporations can be

Bank Exit from Monitoring and Control' (2005) 2(4) *International Journal of Disclosure and Governance* 357.

¹⁰² Franks and Mayer, above n 101, Table 1.

¹⁰³ Ibid 950. Franks and Mayer explained that German corporations were traditionally required to disclose holdings in excess of 25 per cent; therefore, some cross-shareholding may have been disguised.

¹⁰⁴ Stefan Prigge, 'The Survey of German Corporate Governance' in Klaus J Hopt et al (eds), *Comparative Corporate Governance – The State of the Art and Emerging Research* (1998) 970.

¹⁰⁵ For the history of German corporate law reform, see Theodor Baums, 'Company Law Reform in Germany' (2003) 3 *Journal of Corporate Law Studies* 181; Ulrich Noack and Dirk Zetzche, 'Corporate Governance Reform in Germany: The Second Decade' (2005) 2005 *European Business Law Review* 1033.

¹⁰⁶ Klaus J Hopt, 'Corporate Governance in Germany' in Klaus J Hopt and Eddy Wymeersch (eds), *Capital Market and Company Law* (2003) 295.

¹⁰⁷ Nowak reported that German market capitalisation was relatively small compared to other stock markets; for instance, market capitalisation as a percentage of GDP in the European countries was 70.7 per cent, in the UK was 152.2 per cent, but in Germany it was only 58.1 per cent. Eric Nowak, 'Investor Protection and Capital Market Regulation in Germany' in Jan Pieter Krahn and Reinhard H Schmidt (eds), *The German Financial System* (2004) 427.

¹⁰⁸ Jeffrey N Gordon, 'Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany' (1998–1999) 5 *Columbia Journal of European Law* 219, 220.

¹⁰⁹ See Franks and Mayer, above n 101.

separated into two – managers and shareholders. In large German listed companies there are three – managers, shareholders, and employees. German labour for historical reasons has a very strong relationship with corporate management and governance. Labour representatives are located in three sites: labour unions, statutory work councils at the plant level, and, supervisory boards.¹¹⁰ These allow German workers to participate in the company's management. As in some other European and Asian systems, German stock corporations have a dual board system – a two-tier system – with a management board (*Vorstand*) and a supervisory board (*Aufsichtsrat*).

The supervisory board was introduced to German law by *Allgemeines Deutsches Handelsgesetzbuch* [Commercial Code] of 1861¹¹¹ with the aim of creating an independent board to control the management board to protect shareholders and the wider public interest.¹¹² The idea of extending the protection beyond the shareholders was expressed by Robert von Mohl in 1856 who feared that large stock corporations could corrupt the enforcement of state regulations and damage the interests of the public and stakeholders, especially labour.¹¹³ The obligation of the supervisory board to consider the benefits of all stakeholders is still recognised.¹¹⁴ Under German law, only stock corporations (*Aktiengesellschaft* “AG”) are required to establish supervisory boards.¹¹⁵ Generally, the form of AG is employed by large corporations whose shares are publicly traded through listing on a stock market.¹¹⁶ In terms of board responsibility, the supervisory board functions independently from the management board.¹¹⁷ The management board is responsible for managing and directing the business corporation.¹¹⁸ The authority of the management board is restricted by the articles of association, the power of the supervisory board, and the power of shareholders’

¹¹⁰ Viet D Dinh, 'Codetermination and Corporate Governance in a Multinational Business Enterprise' (1998–1999) 24 *The Journal of Corporation Law* 976, 978.

¹¹¹ Jean J Du Plessis and Ingo Saenger, 'The Supervisory Board as Company Organ' in Jean J Du Plessis et al (eds), *German Corporate Governance in International and European Context* (2007) 65.

¹¹² Klaus J Hopt, 'The German Two-Tier Board: Experience, Theories, Reforms' in Klaus J Hopt et al (eds), *Comparative Corporate Governance: The State of the Art and Emerging Research* (1998) 230.

¹¹³ *Ibid* 231.

¹¹⁴ Du Plessis and Saenger, above n 111, 101.

¹¹⁵ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) §§ 1, 95–116.

¹¹⁶ Hannes Schneider and Martin Heidenhain, *The German Stock Corporation Act* (2nd ed, 2000) 3.

¹¹⁷ The detailed discussion on this issue is in Chapter 5.

¹¹⁸ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 76(1).

meetings.¹¹⁹ The members of the management board are required to perform their duties with care and diligence.¹²⁰

The supervisory board has authority to manage the business of the board.¹²¹ Its core power is to supervise the management board.¹²² This covers the appointment and termination of the management board,¹²³ determination of the remuneration of members of the management board,¹²⁴ supervision of the management board,¹²⁵ and, oversight of the business of the corporation.¹²⁶ One of the significant powers of the supervisory board is to approve some specific transactions.¹²⁷ This allows the supervisory board to overturn some decisions of the management board. The articles of association or the supervisory board may determine which transactions may be entered only with the consent of the supervisory board. However, if the supervisory board refuses to give consent, the management board may request a shareholders' meeting resolution to give such consent instead. The function of the supervisory board may be seen as beneficial to minority shareholders because it oversees the management board on behalf of all stakeholders and at the company's expense. In regard to the composition of the supervisory board, generally it consists of representatives of both shareholders and workers.¹²⁸

¹¹⁹ Ibid § 82(2).

¹²⁰ Ibid § 93(1).

¹²¹ See Du Plessis and Saenger, above n 111, Section 3.3.3.1, 3.3.3.2.

¹²² *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 111(1).

¹²³ Ibid § 84.

¹²⁴ Ibid § 87.

¹²⁵ Ibid § 111(1).

¹²⁶ See, eg, ibid §§ 90, 111.

¹²⁷ Ibid § 111(4).

¹²⁸ The composition of the supervisory board in a company in the coal, iron, and steel industries is required to have representatives of shareholders, employees, and one additional member. For other corporations with between 501 and 1,999 employees, it is required to have one-third of the supervisory board occupied by employees. Lastly, the corporations with over 2,000 employees comprise an equal number of representatives of shareholders and employees. See *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 96; *Montan-Mitbestimmungsgesetz* of 1951 [Coal, Iron and Steel Industry Co-Determination Act] (Germany); *Betriebsverfassungsgesetz* of 1952 [Works Constitution Act] (Germany).

2.4.2 Co-determination

The participation of employees in managing the company is referred to as “co-determination” (*Mitbestimmung*).¹²⁹ The model of co-determination was first considered in 1848 in a draft law introduced in a workers’ convention in Berlin, on the establishment of factory committees with participatory rights was considered.¹³⁰ The draft law, which was not enacted, reorganised workers’ participation. Since then, such a model has been revised and influenced by both liberal and national socialist theorists.¹³¹ However, during the Nazi period, all forms of employee participation were abolished, but in 1951, parity co-determination on the supervisory board level re-emerged. Du Plessis and Sandrock explained that the concept of supervisory co-determination was brought back by British occupation authorities and German trade unionists to better protect German democratic traditions and remove some of the appeal of communism.¹³² Having labour and management working together would decrease the divergence between classes in society.¹³³ For large corporations with more than 2,000 workers the size of the supervisory board depends on the number of the corporation’s employees.¹³⁴ The labour representatives are from both blue- and white-collar workers with a specific number of labour seats imposed by the *Mitbestimmungsgesetz* of 1976 [Co-determination Act].¹³⁵ The other significant character of the supervisory board is the election of the chairperson and the vice-chairperson, with a two-third majority of the

¹²⁹ The character of co-determination can be separated into two levels: management co-determination and social co-determination. The first level exists at the shop-floor level, such as works councils, safety committees, and productivity committees. The second level is at the supervisory board. Jean J Du Plessis and Otto Sandrock, 'The German System of Supervisory Codetermination by Employees' in Jean J Du Plessis et al (eds), *German Corporate Governance in International and European Context* (2007) 111–2.

¹³⁰ Heiner Michel, *Co-determination in Germany: The Recent Debate* (2007) Johann Wolfgang Goethe-Universität Frankfurt <<http://www.uclouvain.be/cps/ucl/doc/etes/documents/WDW004.pdf>> at 20 March 2012, 4.

¹³¹ Ibid.

¹³² Plessis and Sandrock, above n 129, 114.

¹³³ Ibid.

¹³⁴ Dinh summarised the character of the supervisory board as follows:

Employees	Total Directors	Labour Directors	Union Directors
Fewer than 10,000	12	6	2
10,000 – 20,000	46	8	2
More than 20,000	20	10	3

Dinh, above n 110, footnote n 49.

¹³⁵ For example, if the company employs fewer than 10,000 workers, the supervisory board should consist of 12 directors, half of whom are held by labour directors. Within the seats designated for employee representatives, trade union representatives should hold at least two seats.

supervisory board's members. If such a majority cannot be attained, shareholder representatives elect the chairperson while the employee representatives elect the vice-chairperson.¹³⁶ Importantly, the chairperson has a double vote to break a tie.¹³⁷ This extra vote is crucial as the chairperson can cast the vote in favour of the shareholders' interest.¹³⁸ Minority shareholders potentially benefit from the co-determination model in many ways. The members of the supervisory board have access to information about the corporate enterprise.¹³⁹ This empowers them as a monitoring organ and may reduce the possibility of the expropriation by managers or large shareholders. In addition, the German approach avoids many disagreements between management and labour. Collective bargaining at the level of both work councils and supervisory boards provides the possibility of cooperative compromises instead of strikes or other actions.¹⁴⁰

Although the roles of the supervisory board and the co-determination model are considered to be mechanisms for controlling the management board and protecting the interests of minority shareholders, the supervisory board is not be able to properly supervise the management.¹⁴¹ In a large corporation, a supervisory board may not have a significant role.¹⁴² This is because the members of the supervisory board have insufficient experience and knowledge to oversee the managers who have considerable expertise in the corporation's business. Another criticism by Franks and Mayer is that shareholders' representatives on the supervisory boards are dominated by large shareholders and banks.¹⁴³ In other words, half of the members of the supervisory board represent larger controlling shareholders, not minority shareholders. In addition, the elected shareholder representatives have a close relationship with the company they

¹³⁶ David H Brody et al, 'Alternatives to the United States System of Labor Relations: A Comparative Analysis of the Labor Relations Systems in the Federal Republic of Germany, Japan, and Sweden' (1988) 41 *Vanderbilt Law Review* 627, 636–7.

¹³⁷ *Mitbestimmungsgesetz* of 1976 [Co-determination Act] (Germany) § 29(2).

¹³⁸ See *ibid*; Herbert Wiedermann, 'Codetermination by Workers in German Enterprises' (1980) 28 *American Journal of Comparative Law* 79, 80.

¹³⁹ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 111(2).

¹⁴⁰ Dinh, above n 110, 982.

¹⁴¹ Ingo Saenger, 'Conflicts of Interest of Supervisory Board Members in a German Stock Corporation and the Demand for Their Independence' (2005) 1(1) *Corporate Governance Law Review* 147.

¹⁴² Du Plessis and Saenger, above n 111, 13.

¹⁴³ Franks and Mayer, above n 101, 952–3.

supervise. This may limit their effective monitoring of management.¹⁴⁴ Roe further argued that the presence of employee representatives also weakened the supervisory board.¹⁴⁵ A German supervisory board meets only two to four times a year.¹⁴⁶ More meetings are likely to improve firm operations and monitoring.¹⁴⁷ But because this would provide a platform for the labour representatives both management and shareholders shy away from more meetings. In the situation where the managers are unmonitored and labour is uninformed, the question arises of how increasing labour power will provide better protection for minority shareholders.

In practice, however, it has been found that co-determination has a negative impact on firm governance because labour representatives tend to pursue only their own interests. It is reported that the main activity of the supervisory board is related to interests particular to the labour side and social matters instead of the actual supervision of business decisions and entrepreneurial planning in the company.¹⁴⁸ In terms of firm valuation, Gorton and Schmid showed that there is a relationship between the firm's value and the allocation of seats in a supervisory board to employee representatives.¹⁴⁹ They reported that the corporations with half labour representatives on the supervisory board traded at a discount of 31 per cent compared with the firms with one-third labour representatives.¹⁵⁰ They also explained that this was the result of the divergent interests between labour and shareholders. Labour representatives may consider the interests of workers rather than that of the shareholders or even the company. For instance, the shareholders might want to restructure the company, reduce wages or possibly lay off some workers to increase the firm's value but such a proposal is likely to be rejected by the labour side as such changes have a negative impact on workers.¹⁵¹

¹⁴⁴ Thomas J Jr Andre, 'Some Reflections on German Corporate Governance: A Glimpse at German Supervisory Boards' (1996) 70 *Tulane Law Review* 1819, 1819.

¹⁴⁵ Mark J Roe, 'German Codetermination and German Securities Market' (1998) 1998 *Columbia Business Law Review* 167.

¹⁴⁶ A listed company is required to have supervisory board meetings twice annually. *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 110(3). However, in practice, some boards prefer to meet four times yearly.

¹⁴⁷ Roe, above n 145, 174.

¹⁴⁸ Hopt, above n 112, 247.

¹⁴⁹ Gary Gorton and Frank A Schmid, 'Capital, Labor, and the Firm: A Study of German Codetermination' (2004) 2(5) *Journal of the European Economic Association* 863.

¹⁵⁰ *Ibid* 895.

¹⁵¹ *Ibid* 889.

Furthermore, there have been current incidents revealing dysfunctionality in the German co-determination model. For instance, after the takeover deal between Mannesmann AG and Vodafone was successfully completed, four members of the committee on the supervisory board of Mannesmann passed a resolution which granted €57 million bonuses for former members of the management and supervisory board.¹⁵² Among the four committee members, one was a labour representative. He was one of the most militant and most powerful German trade unionists and one would have expected that he would have objected to such a proposal.¹⁵³ On the contrary, due to the close relationship between the management and the supervisory boards, he abstained from voting and let the resolution pass. This event raises serious questions about the effectiveness of labour representatives and their role in protecting minority shareholders.

2.4.3 The role of German banks

In addition to the supervisory board and co-determination, another significant feature is the role of German banks.¹⁵⁴ Under the concept of *Grossbanken* (big banking houses), German banks are allowed to engage in both commercial and investment businesses. They are able to hold shares in a company directly or indirectly through an investment company.¹⁵⁵ In addition, banks can participate as a custodian holding shares on behalf of customers.¹⁵⁶ For fees banks manage their shares, make recommendations on voting, and vote.¹⁵⁷ Combining the voting power from their own shares, shares held by their investment companies, and deposited shares, banks have large blocks of shares in German corporations.

¹⁵² Justus Leicht, *Germany: Mannesmann Execs Acquitted in Corruption Trial* (2004) World Socialist Web Site <<http://www.wsws.org/articles/2004/aug2004/mann-a04.shtml>> at 20 March 2012.

¹⁵³ Du Plessis and Sandrock, above n 129, 132–3.

¹⁵⁴ Fukuyama explained that German banks played a significant role in German industrial growth. German businesses generally received funds from banks, rather than public offerings. The banks also had a close connection with the businesses they invested in. Francis Fukuyama, *Trust: The Social Virtues and the Creation of Prosperity* (1995) 312.

¹⁵⁵ John C Coffee Jr, 'The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control' (2001) 111 *The Yale Law Journal* 1, 53.

¹⁵⁶ Theodor Baums, 'Corporate Governance in Germany: The Role of the Banks' (1992) 40 *The American Journal of Comparative Law* 503, 506–7.

¹⁵⁷ The detailed discussion on this issue is in Chapter 4.

Several researchers have reported the strong influence of banks on companies. According to Frank and Mayer, the ultimate shareholders of German listed companies in the early 2000s were families and banks.¹⁵⁸ Bank shareholdings accounted for approximately 12 per cent of German stock corporations. Another study showed that, on average, banks represent 82.67 per cent of all votes that were presented at the shareholder meetings.¹⁵⁹ Therefore, the shareholder members of the supervisory board were likely to be elected by the banks. In 1998 the nine largest banks held seats in the supervisory boards of 94 out of the 100 largest German firms.¹⁶⁰ At the firm level, the study reported that some members of the management boards of those banks also sat on the supervisory boards of the *Deutsche Aktienindex* (DAX) 30.¹⁶¹ Out of the DAX30, there were 24 non-financial corporations and 19 of these 24 firms had members from the management board of Deutsche Bank on their supervisory boards. Members of the management boards of Dresdner Bank and Commerzbank represented 10 and six supervisory boards of these 24 firms respectively. From these 24 corporations, only three companies¹⁶² had no representatives from any banks holding a position on the supervisory boards.¹⁶³

This presence of banks may benefit minority shareholders in different ways. First of all, through its direct interest in the firm as a shareholder, proxyholder, and lender, a bank has a strong incentive to monitor the management board. As a shareholder, the bank oversees the managers to ensure that their equity is well protected.¹⁶⁴ The right to vote as a proxyholder also strengthens the bank's power. As a lender, it has access to inside information. This reduces the problem of asymmetric information generally faced by creditors.¹⁶⁵ In addition to their incentive to monitor the company, bank representatives have a specialised knowledge, especially in the financial field, to effectively monitor

¹⁵⁸ Franks and Mayer, above n 101, 950.

¹⁵⁹ Baums, above n 156, 507.

¹⁶⁰ Andre, above n 144, 1837. Among German banks, the largest shareholdings in private firms were Deutsche Bank, Dresdner Bank and Commerzbank. Peter O Mülbert, 'Bank Equity Holding in Non-Financial Firms and Corporate Governance' in Klaus J Hopt et al (eds), *Comparative Corporate Governance: The State of the Art and Emerging Research* (1998) 450.

¹⁶¹ These firms are considered as the publicly-traded companies that have no dominant shareholders. Andre, above n 144, 1837.

¹⁶² Which are BMW, Deutsche Babcock, and MAN.

¹⁶³ Andre, above n 144, 1383.

¹⁶⁴ Baums, above 156, 516.

¹⁶⁵ Ibid 517.

management. The banks also have a large number of staff to support their representatives. Moreover, with their broad knowledge of the market in managers, the banks can elect to the board people who have a deep understanding and experience of management.¹⁶⁶

Although the potential roles of banks in protecting minority shareholders are clear, some scholars criticise the power banks possess. The relationship between banks and companies allows the banks to acquire information, to participate in the shareholders' meeting, and to monitor the management. The conflict of interest possibly occurs. As Vagts argued:

As a depositary of a corporation's funds, the bank may wish to keep the firm from withdrawing its deposits into other uses. As underwriter for the company, it may vote for a new stock issue which disinterested analysts would find unnecessary. As creditor of the company, it may prefer to see its debtor's earnings retained to give it additional security rather than paid out as dividends to the shareholders it is supposed to represent. ... How can they advise individual client-shareholders on buying and selling shares, protect their own shareholders by maintaining good relations with corporate managers and defending their interests as creditors and underwriters, and also act as voting representatives?¹⁶⁷

Also, the banks' representatives have no real interest in the companies they control. This problem is similar to the agency problem in the US when the managers, who initiate and implement a decision that affects the residual claimants ie the shareholders, do not bear any of the risks from such a decision.¹⁶⁸ Bank representatives have a strong influence over a company through the general meeting, the supervisory board, and the management board without bearing any risks themselves. Therefore, it is debatable whether the banks' role actually benefits or harms other shareholders. The relationship between the bank and corporate management is very close. Because of its position as a "house bank", the bank will be unlikely to confront the management and generally

¹⁶⁶ Ibid 513.

¹⁶⁷ Detler F Vagts, 'Reforming the "Modern" Corporation: Perspectives from the German' (1966) 80(1) *Harvard Law Review* 23, 57, 63.

¹⁶⁸ See Fama and Jensen, above n 3; Fama and Jensen, above n 37.

attempts to settle issues behind the scenes with the management board. In fact, the banks:

[S]it silently through general assembly discussion and then vote with management. One does see, from time to time, that the [bank] of a given corporation has intervened in its affairs, generally when it is faced by drastically adverse circumstances.¹⁶⁹

Studies of the interrelation between bank shareholdings and a firm's performance are inconclusive.¹⁷⁰ Therefore, it is uncertain whether a bank's participation has a positive impact on firm governance.

In all, the above analysis indicates that corporate governance in the US and German models are significantly different. In the US, the development of minority shareholders' protection is based on the perceived problem of agency. Different organs and mechanisms are created to maintain the balance of power between managers and shareholders. The management is controlled by capital markets and dispersed shareholders.¹⁷¹ Shareholders who are not satisfied with the outcome of the management's decision may "vote with their feet" – by selling their shares.¹⁷² The German corporate governance model has evolved through German history reflecting its economic and social contexts to rely on mechanisms located inside the company. The fundamental principle behind the supervisory board, co-determination, and bank control is the protection of stakeholders. Such divergences are impossible to reconcile into a single model of corporate governance. Due to such differences, it is uncertain which approach is more suitable for Thailand to adopt to further develop its legal framework on minority shareholders' protection. There may be business and cultural factors in Thailand that could substitute for either the US or the German model.

2.5 The concept of minority shareholders' protection in the East Asian context

As indicated, the work of Berle and Means has influenced finance literature on large modern US corporations. However, attention to the ownership structure of firms has

¹⁶⁹ Vagts, above n 167, 58.

¹⁷⁰ See, eg, Mülbert, above n 160, F.III.

¹⁷¹ Richard Ziolkowski, *A Re-examination of Corporate Governance: Concepts, Models, Theories, and Future Directions* (PhD Thesis, University of Canberra, 2005) 286.

¹⁷² Ibid.

expanded since the publications by La Porta *et al* that point to a contradiction in the role of companies in the creation of national wealth.¹⁷³ They observed the ownership structure of the 20 largest publicly-traded firms in each of the 27 richest countries. Their observations revealed that shares of 36 per cent of the top 20 firms in those 27 countries were widely held.¹⁷⁴ They further reported that, only in the US, the United Kingdom and Japan,¹⁷⁵ did widely held corporations predominate, elsewhere large corporations usually had controlling shareholders – wealthy families or governments.¹⁷⁶ Claessens, Djankov, and Lang conducted a similar study in Asian countries.¹⁷⁷ They investigated 2,980 corporations in nine East Asian countries¹⁷⁸ and found that more than half of those firms were controlled by a single shareholder, mainly a family.¹⁷⁹ Any conflict within an Asian corporation is thus likely to be the result of the divergent interests of controlling and minority shareholders rather than of strong managers and weak shareholders as described by Fama and Jensen.¹⁸⁰ Following in this section, the ownership structure of East Asian corporations and the conflict between controlling and minority shareholders are discussed.

2.5.1 Ownership structure of East Asian corporations

As indicated, the study by Claessens, Djankov, and Lang revealed that more than 50 per cent of East Asian corporations were owned by families.¹⁸¹ In Thailand, for example, families controlled approximately 61.6 per cent of publicly-traded corporations while

¹⁷³ La Porta, Lopez-de-Silanes and Shleifer, above n 9.

¹⁷⁴ Ibid 491.

¹⁷⁵ Though companies are less concentrated, Prowse indicated that commercial banks owned more than 20 per cent of the outstanding stocks of listed firms. Stephen D Prowse, 'The Structure of Corporate Ownership in Japan' (1992) 47(3) *The Journal of Finance* 1121, 1123. For details on the governance structure of Japanese corporations, see Erik Berglöf and Enrico Perotti, 'The Governance Structure of the Japanese Financial Keiretsu' (1994) 36 *Journal of Financial Economics* 259.

¹⁷⁶ Ibid 491–6.

¹⁷⁷ Stijn Claessens, Simeon Djankov and Larry HP Lang, 'Who Controls East Asian Corporations?' (Policy Research Working Paper No 2054, World Bank, 1999) 3.

¹⁷⁸ Which are Hong Kong, Indonesia, Japan, South Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand.

¹⁷⁹ Claessens, Djankov, and Lang, above n 177, front page, 3. In other countries, such as France, Italy, Korea, and Sweden, the median largest voting blocks were around 30 to 60 per cent and corporations were normally dominated by families. Organisation for Economic Co-operation and Development, *Corporate Governance: A Survey of OECD Countries* (2004) 31–3.

¹⁸⁰ The detailed discussion on the “agency problem” was discussed earlier in Section 2.3.

¹⁸¹ Claessens, Djankov and Lang, above n 1, Table 6.

widely held corporations accounted for only 15.3 per cent.¹⁸² Claessens, Djankov, and Lang further considered how concentrated family control was in those companies by calculating the total value of listed corporation assets owned by the largest 15 families in each country. They reported that a large proportion of those assets were in the hands of a small number of families. For instance, in Thailand, Indonesia and the Philippines, the 15 largest families controlled more than half of the total value of corporate assets (53.3, 61.7, and 55.1 per cent respectively).¹⁸³ On the other hand, founding American families in the S&P 500 owned only 18 per cent of their firms outstanding equity.¹⁸⁴ The findings suggest that a small number of families have a control over most East Asian corporations.

These wealthy families employ different patterns of ownership structures to maintain control over corporations. One of the common patterns is the pyramidal corporate structure.¹⁸⁵ The study by Claessens, Djankov, and Lang found that a pyramid structure was widely applied in Indonesia (66.9 per cent of publicly-traded firms) but less so in Thailand (12.7 per cent of publicly-traded firms).¹⁸⁶ In addition to the pyramidal structure, the other structure protecting such ownership is by cross-holdings.¹⁸⁷ In East Asian countries, the highest level of cross-ownership is found in Singapore (15.7 per cent of publicly-traded firms) and the lowest in Thailand (0.8 per cent of publicly-traded firms).¹⁸⁸

¹⁸² Ibid.

¹⁸³ Ibid Table 9.

¹⁸⁴ Anderson and Reeb, above n 39. 1302.

¹⁸⁵ Randall Morck, Daniel Wolfenzon and Bernard Yeung, 'Corporate Governance, Economic Entrenchment, and Growth' (2005) 43(3) *Journal of Economic Literature* 655, 663. For example, Family X holds 50 per cent plus one share in Company A and the remaining 50 per cent minus one share are divided among small public shareholders. In the second tier, Company A holds 50 per cent plus one share in Company B and the remaining shares are held by small public shareholders. In the third tier, Company B owns 50 per cent plus one share in Company C and the rest of the shares are again held by public shareholders. In this case, Family X has control over Company C as, along the control chain, it holds more than 50 per cent of shares of Company A and B while it actually owns only 12.5 per cent [(50%)(50%)(50%)] of Company C's cash-flow rights.

¹⁸⁶ Claessens, Djankov, and Lang, above n 1, 93.

¹⁸⁷ From the above example, Company C may have cross-holdings if it holds a share of any companies along the chain of control. Suppose that Company C has 25 per cent of voting rights in firm A, Family X has 56.25 per cent of the control rights in firm A, 50 per cent directly and 6.25 per cent [(50%)(50%)(25%)] through a cross-holding structure.

¹⁸⁸ Ibid Table 3.

The other significant structure of Asian corporations is the “family business group”.¹⁸⁹ A business group refers to ‘a collection of legally independent firms that are bound by economic (such as ownership, finance, and commercial) and social (such as family, kinship, and friendship) ties’.¹⁹⁰ A family business group contains a number of family-controlled companies or affiliations.¹⁹¹ The family maintains control over the group both through pyramidal and cross-holding structures and the appointment of family members in the highest management positions.¹⁹² In these family-controlled companies it is difficult to find a core group business. The focus is not on one industry but many through lots of small companies.¹⁹³ Consequently, the companies in the group are largely diversified and unorganised.¹⁹⁴ Ghemawat and Khanna suggested that such a diversified structure allows the corporations to exert their market power in different markets,¹⁹⁵ to share common resources, such as supplier relationships, customers, or technology, and to allocate internal capital within the group.¹⁹⁶

In regard to the management of the family business group, controlling shareholders tend to appoint family members to executive positions in key firms across the group.¹⁹⁷ Claessens, Djankov and Lang examined the management of East Asian companies and found that the highest level positions in about 60 per cent of companies with

¹⁸⁹ Wiwattanakantang, above n 27 [the equity ownership structure], 12; Michael N Young et al, 'Corporate Governance in Emerging Economies: A Review of the Principal-Principal Perspective' (2008) 45(1) *Journal of Management Studies* 196, 205–7.

¹⁹⁰ Daphne Yiu, Garry D Bruton and Yuan Lu, 'Understanding Business Group Performance in an Emerging Economy: Acquiring Resources and Capabilities in Order to Prosper' (2005) 42(1) *Journal of Management Studies* 183, 183.

¹⁹¹ Wiwattanakantang, above n 27 [the equity ownership structure], 12.

¹⁹² Akira Suehiro, 'Family Business Re-assessed: Corporate Structure and Late-Starting Industrialization in Thailand' (1993) *The Developing Economies* 378, 378.

¹⁹³ Michael Backman, *Asian Eclipse: Exposing the Dark Side of Business in Asia* (1999) 66.

¹⁹⁴ Ibid 65. Beckman described the structure of Asian conglomerates as follows:

What does it take to make a conglomerate in Asia? There is a fairly standard recipe. Take a bank, add some trading interests, some manufacturing interests, a stock-broking firm, lots of real estate holdings, and perhaps a hotel, mix it all around to form a loose structure but one in which lots of internal transactions take place, list some but not all of the companies on the local stock exchange, and put the lot under the control of one family.

¹⁹⁵ See Tarun Khanna and Yishay Yafeh, 'Business Groups and Risk Sharing Around the World' (2005) 78(1) *Journal of Business* 301, 333.

¹⁹⁶ See Pankaj Ghemawat and Tarun Khanna, 'The Nature of Diversified Business Groups: A Research Design and Two Case Studies' (1998) 46(1) *The Journal of Industrial Economics* 35, 36–42. See also Heitor Almeida and Daniel Wolfenzon, 'A Theory of Pyramidal Ownership and Family Business Groups' (2006) 61 *The Journal of Finance* 2637.

¹⁹⁷ Morck, Wolfenzon and Yeung, above n 185, 665.

concentrated-ownership structures were held by family members.¹⁹⁸ In Thailand, in particular, Wiwattanakantang observed the relationship between the control and management of Thai listed companies and reported that more than 75 per cent of family-controlled firms had family members involved in the management and control of the firms.¹⁹⁹ To retain control over the group, the families preferred placing family members or trusted associates in the business group rather than delegating their power to professional managers who were considered outsiders.²⁰⁰

In addition to the complex structure of family business groups, another outstanding character of East Asian companies is that of a close relationship with banks. It is common in East Asian countries to find a bank in a conglomerate of companies engaged in non-banking activities.²⁰¹ In Thailand, for example, the Thai Farmer Bank or Kasikorn Bank, after rechristening, one of Thailand's biggest banks, was founded by the Lamsam family whose business included not only a range of financial service companies but also exporting, warehousing, and agri-processing.²⁰² Beckman observed that having a bank in a business group benefited the conglomerate as it was a source of income to fund the founders' own projects.²⁰³ For a business group in which a bank is not a part, the connection between a banker and a founder of a business is vital as it facilitates corporate financing. However, the bankers often give preference to projects promoted by their friends, relatives, or a trusted people without appropriately considering the quality of the project as they may receive private benefits from the borrower and believe that any possible losses will be covered by the government in a bailout.²⁰⁴

¹⁹⁸ Claessens, Djankov and Lang, above n 177, 94.

¹⁹⁹ Wiwattanakantang, above n 27 [the equity ownership structure], 19.

²⁰⁰ Cally Jordan, 'Family Resemblances: The Family Controlled Company in Asia and its Implications for Law Reform' (1997) 8 *Australian Journal of Corporate Law* 1, 7–8.

²⁰¹ Beckman, above n 193, Chapter 6. In Indonesia, before the 1997 financial crisis, there were more than 240 private banks and most of them were part of a business group. Benny Tabalujan, 'Corporate Governance of Indonesian Banks: The Legal & Business Contexts' (2001) 13 *Australian Journal of Corporate Law* 67, 77, 84–5.

²⁰² Ibid.

²⁰³ Beckman, above n 193, Chapter 6. See also Randall S Kroszner and Philip Strahan, 'Bankers on Boards: Monitoring, Conflicts of Interest and Lender Liability' (Working Paper No W7319, NBER, 2001).

²⁰⁴ Yupana Wiwattanakantang, Raja Kali and Chutatong Charumilind, 'Crony Lending: Thailand before the Financial Crisis' (CEI Working Paper No 2002-4, Center for Economic Institutions, Institute of Economic Research, Hitotsubashi University, 2002) 2.

These findings suggest that the ownership of listed companies in East Asian countries is highly concentrated in the hands of extremely wealthy individuals or families. Using pyramidal and cross-holding structures, controlling shareholders of those companies have almost absolute power over the corporations in their business groups and extend their control to a large part of the economy. These ownership patterns are found across East Asian countries regardless of their legal systems.²⁰⁵ In the next section, the impact of this disproportionate control on minority shareholders will be discussed.

2.5.2 The effect of concentrated-ownership structure

The incentive of controlling shareholders to maximise their firms' values is strong as they have a large ownership stake in a corporation.²⁰⁶ Some degree of concentration of ownership can bring about value-increasing changes in corporate policies because large shareholders have a strong incentive to monitor managers.²⁰⁷ This benefits small shareholders as large shareholders incur the cost of monitoring and small shareholders can free-ride on their effort.²⁰⁸ As well, controlling shareholders can effectively monitor management as they have sufficient voting powers to remove incompetent managers.²⁰⁹ The role of controlling shareholders obviously minimises the risk of agency problems – the conflict between managers and shareholders.²¹⁰ Several studies affirm that firms with concentrated-ownership structures operate more efficiently and profitably. Alba *et al* compared the performance of Thai firms in 1992 and 1996, before and after concentrated ownership was significantly diluted, and found that 'ownership concentration [was] positively (and significantly) related to profitability in 1992' but the performance had turned negative by 1996.²¹¹ Furthermore, the structure of the group allows group-affiliated firms to share resources, such as technological skills and

²⁰⁵ See Claessnes, Djankov, and Lang, above n 1.

²⁰⁶ Shleifer and Vishny, above n 100, 754.

²⁰⁷ Jeremy Edwards and Alfons J Weichenrieder, 'Ownership Concentration and Share Valuation' (2004) 5(2) *German Economic Review* 143, 165.

²⁰⁸ Free-rider problem occurs because the monitor costs only the monitoring shareholder but benefits all shareholders equally. Therefore, a shareholder is reluctant to take actions in the hope that others will.

²⁰⁹ Edwards and Weichenrieder, above n 207, 165.

²¹⁰ See Jensen and Meckling, above n 35.

²¹¹ Pedro Alba, Stijn Claessens and Simeon Djankov, 'Thailand's Corporate Financing and Governance Structure' (Policy Research Working Paper No 2003, World Bank, 1998) 18.

knowledge.²¹² Also, corporations within the group can financially operate without relying on the ineffective external capital market.²¹³ In regard to these benefits, the group structure is widely found in developing markets as it assists the group to minimise transaction costs.²¹⁴

Although the advantages of the concentrated-ownership structure are recognised, it should be borne in mind that controlling shareholders often have control over corporations while their entitlement to dividends and rights in the cash flow are lower than their control rights. Claessens *et al* found that the separation of ownership and control was high in Japan, Indonesia, and Singapore and low in the Philippines and Thailand.²¹⁵ For instance, a large shareholder in one Japanese company had ultimately 10 votes while directly holding only six shares. In Thailand, for 10 ultimate votes, a large shareholder generally owned 9.5 shares.²¹⁶ This separation of control and cash-flow rights can create an agency problem. On the one hand, through their control rights, controlling shareholders have a direct influence over corporate operations. On the other hand, they may have less incentive to maximise a firm's value as they are likely to prioritise their own interests that may not benefit other shareholders.²¹⁷ Several studies affirm that highly concentrated ownership facilitates expropriation of wealth from minority shareholders. Claessens *et al* studied the relationship between firm value on the one hand, and cash flow and control rights on the other. They found that firm valuation increased when cash-flow ownership was in the hands of the largest shareholder; however, the increase of control rights decreased the firm value.²¹⁸ These findings suggest that when the control rights are excessive in relation to cash-flow rights, there is the risk of expropriation of minority shareholders by controlling shareholders.²¹⁹ Faccio, Lang, and Young studied the relationship between dividend

²¹² Sea-Jin Chang and Jaebum Hong, 'Economic Performance of Group-Affiliated Companies in Korea: Intragroup Resource Sharing and Internal Business Transactions' (2000) 43(3) *The Academy of Management Journal* 429, 432.

²¹³ *Ibid* 435–6.

²¹⁴ *Ibid* 445.

²¹⁵ Stijn Claessens *et al*, 'Expropriation of minority shareholders: Evidence from East Asia' (Policy Research Working Paper No 2088, World Bank, 1999) Table 1.

²¹⁶ *Ibid* Table 4.

²¹⁷ Shleifer and Vishny, above n 100, 758.

²¹⁸ Stijn Claessens *et al*, 'Disentangling the Incentive and Entrenchment Effects of Large Shareholdings' (2002) 57(6) *The Journal of Finance* 2741, 2769–70.

²¹⁹ *Ibid* 2770.

payouts and expropriation of minority shareholders by controlling shareholders. Dividend distribution reflects the level of expropriation as it transfers corporate wealth away from insider control. The result showed that the dividend rate in Asia was lower than elsewhere. In other words, insiders in Asian corporations prefer to retain dividends under their control and this suggests high expropriation in Asian firms by controlling shareholders.

Due to their considerable control over a company, controlling shareholders are able to benefit at the minority shareholders' expense in different ways. Dominant shareholders may position family members, relatives or trusted associates in executive levels of the firm. Although the performance of such officers is unsatisfactory, controlling shareholders will be unlikely to remove them.²²⁰ Furthermore, controlling shareholders who hold an executive position with the firm can abuse their authority by approving high remuneration for themselves or transferring resources from the firm for their benefit through self-dealing transactions.²²¹ Documenting expropriation across East Asian countries, Johnson *et al* found that in most incidents managers of the firms moved some cash and other assets out of their company to repay their own debts, to finance offshore companies under their control, or to bail out financially troubled parent companies.²²² The managers can easily make these transfers as they are also the controlling shareholders.²²³ When a company in a pyramidal structure is listed on the stock market, it is required to publish annual reports and disclose related information to the market. However, the provided information does not reflect a picture of the group but only that of the listed company.²²⁴ The controlling families also prefer to keep information within the family so that they can take advantage of the lack of transparency. In Indonesia, for example, the most profitable assets are normally located in a privately owned company while the publicly-traded companies generate an income

²²⁰ Micheal S Gibson, 'Is Corporate Governance Ineffective in Emerging Markets?' (Working Paper No 99-63, Federal Reserve Board FEDS, 2002) 23-4; Yves Bozec and Richard Bozec, 'Ownership Concentration and Corporate Governance Practices: Substitution or Expropriation Effects?' (2007) 24 *Canadian Journal of Administrative Sciences* 182, 184.

²²¹ Simon Johnson et al, 'Tunneling' (2000) 90 *The American Economic Review* 22, 22.

²²² Simon Johnson et al, 'Corporate Governance in the Asian Financial Crisis' (2000) 58 *Journal of Financial Economics* 141, Table 1. This incident occurred in Thailand. See Deunden Nikomborirak, 'Corruption in the Business Sector and Corporate Governance in Thailand' (TDRI Report No 29, Thailand Development Research Institute, 2001) 2.

²²³ Johnson, above n 222, 143.

²²⁴ Backman, above n 193, 68.

from the public for the group.²²⁵ These firms voluntarily improve firm-level governance only to attract external capital providers.²²⁶

Examining the impact of the ownership structure on stock price performance in five East Asian countries²²⁷ during the 1997 financial crisis, Mitton reported that the firms that had high inside ownership concentration normally had worse stock price performance because large shareholders that were involved in management had an opportunity to exploit minority shareholders' wealth.²²⁸ Lemmon and Lins also affirmed that during the crisis, while the firm's investment opportunity decreased, the incentives of controlling shareholders to expropriate minority shareholders increased.²²⁹ The study also showed that the return from stocks of family-controlled firms was 10 to 20 per cent lower than those of others.²³⁰ In Korea, studying the performance of Korean business groups, Chang revealed that there was no evidence showing the relationship between concentrated ownership and firm performance.²³¹ On the contrary, he found strong evidence that controlling shareholders tended to increase their stake in profitable firms and later transferred profits from such firms to their privately owned corporations through intergroup trade.²³² In respect of Thai firms, Wiwattanakantang found that firms with controlling shareholders performed well²³³ as a pyramidal structure was less applied in Thailand.²³⁴ However, when controlling shareholders were involved in the management, a negative effect was detected and such an effect became greater when controlling-and-manager shareholders' ownership represented 25 to 50 per cent of firm

²²⁵ Ibid 68–9.

²²⁶ Chandrasekhar Krishnamurti, Aleksandar Šević and Željko Šević, 'Legal Environment, Firm-level Corporate Governance and Expropriation of Minority Shareholders in Asia' (2005) 38 *Economic Change and Restructuring* 85.

²²⁷ Indonesia, Korea, Malaysia, the Philippines, and Thailand.

²²⁸ Todd Mitton, 'A Cross-Firm Analysis of the Impact of Corporate Governance on the East Asian Financial Crisis' (2002) 64(2) *Journal of Financial Economics* 215, 215, 229.

²²⁹ Michael L Lemmon and Karl V Lins, 'Ownership Structure, Corporate Governance, and Firm Value: Evidence from the East Asian Financial Crisis' (2003) 58(4) *The Journal of Finance* 1445, 1466.

²³⁰ Ibid.

²³¹ Sea-Jin Chang, 'Ownership Structure, Expropriation, and Performance of Group-Affiliated Companies in Korea' (2003) 46(2) *The Academy of Management Journal* 238, 250.

²³² Ibid 241.

²³³ Consistently, Suehiro found a positive relationship between ownership structure and firm performance. Akira Suehiro, 'Family Business Gone Wrong? Ownership Patterns and Corporate Performance in Thailand' (ADB Institute Working Paper No 19, Asian Development Bank Institute, 2001).

²³⁴ Yupana Wiwattanakantang, 'Controlling Shareholders and Corporate Value: Evidence from Thailand' (2001) 9 *Pacific-Basin Financial Journal* 323, 359. Claesens, Djankov, and Lang also reported little separation between cash-flow and control rights of the ownership structure in Thai firms. Claesens, Djankov, and Lang, above n 177.

stocks.²³⁵ Kim, Kitsabunnarat and Nofsinger also observed the negative operating performance of Thai firms after the firms became public.²³⁶ Bertrand *et al* examined how family structure affected corporate structure and firm performance. They found that the founders of a firm tended to appoint their sons rather than outside managers.²³⁷ The number of sons²³⁸ of the founder was also associated with the number of companies in the pyramidal structure.²³⁹ The result further indicated that the family business groups that had many sons owning fractions of the group performed more poorly than those with fewer sons.²⁴⁰

In companies with highly concentrated, expropriation of benefits from minority shareholders generally occurs.²⁴¹ It is therefore important to find ways to ensure that the benefits of minority shareholders will not be exploited by controlling shareholders. Underlying this is the more fundamental question: how to distribute and balance the power of corporate control between majority and minority shareholders. In other words, the problem is how to make majority shareholders free to enjoy their control but ensure that their actions are not unfair to minority shareholders' interests.

2.5.3 The application of Western corporate governance models

The differences between US, German, and East Asian listed corporations in the above analysis may be summarised as follows:

²³⁵ Ibid. Cf Morck, Shleifer and Vishny, above n 39. Morck, Shleifer and Vishny developed a model to examine the relationship between management ownership and market valuation. They reported that the value of the firm rises when board ownership increased from 0 per cent to 5 per cent but fell when the managerial ownership rose further. However, it increased again when board ownership rose beyond 25 per cent.

²³⁶ Kenneth A Kim, Pattanaporn Kitsabunnarat and John R Nofsinger, 'Ownership and Operating Performance in an Emerging Market: Evidence from Thai IPO Firms' (2004) 10 *Journal of Corporate Finance* 355, 374–5.

²³⁷ Marianne Bertrand et al, 'Mixing Family with Business: A Study of Thai Business Groups and the Families behind them' (2008) 88(3) *Journal of Financial Economics* 466, 479.

²³⁸ The authors pointed out that, in Thai corporations, there was a negative relationship between the number of sons and firm performance; however, the study did not find a significant effect of such a relationship between the numbers of daughters and firm performance. Ibid 479.

²³⁹ Ibid 481.

²⁴⁰ Ibid 485.

²⁴¹ Dhnadirek and Tang suggested that to strengthen the Thai corporate governance system, there should be a mechanism for limiting ownership concentration. Rachana Dhnadirek and John Tang, 'Corporate Governance Problems in Thailand: Is Ownership Concentration the Cause?' (2003) 10(2) *Asia Pacific Business Review* 121.

Table 2.1 Characters of the US, German and East Asian corporations

Traits	US corporations	German corporations	East Asian corporations
Share ownership	Diffused	Concentrated	Concentrated
Controlling shareholders	Negligible	Banks and wealthy families	Wealthy families
Pyramid structure	Rare	Widely employed	Widely employed
Cross-shareholding	Negligible	Significant	Significant
Management	Professional managers	Representatives of shareholders and employees	Family members, relatives, and trusted associates
Influence of management	Strong	Strong	Weak
Relationship with banks	Arm's length transactions	Strong	Strong
Market for corporate control	Active	Negligible	Negligible

Source: Author's compilation

The characters of East Asian listed corporations follow a pattern similar to those of German corporations but different from those of US corporations. This raises questions whether mechanisms applied in the US and Germany can provide effective protection for minority shareholders in the East Asian context. Given the similar characters of the US, German, and East Asian corporations, it may be argued that minority shareholders' protection found in German law and practice may be more suitable for East Asian countries than those of the US.

In US, the key mechanisms to protect minority shareholders' interests are insider shareholding, shareholding by blockholders, institutional shareholdings, the use of outsiders on the board of directors, external labour markets for managers, and markets for corporate control. For East Asian corporations, encouraging managers to hold shares in a company is unlikely to improve its governance. As mentioned above, in East Asian corporations, members of the board of directors are normally members of the family that holds the majority shares of the company. Conflict between managers and shareholders will be unlikely to occur as the family-member managers act in the family's interests which coincide with their own interests. In this context, managerial shareholdings therefore do not provide any additional protection for minority

shareholders. In the US, it is believed that shareholding by blockholders may benefit minority shareholders as large shareholders have a strong incentive to monitor management. However, such a mechanism is likely to make the protection for minority shareholders in East Asian corporations worse.²⁴² As indicated, a root cause of the expropriation of minority shareholders is the concentrated ownership structure; therefore, increasing ownership concentration increases the power of controlling shareholders to exploit the benefit of the minority. Another internal mechanism commonly used in the US is the appointment of outsiders to the board of directors. The outsiders are intended to balance the power of managers and to ensure that the benefits of shareholders are protected. Such outside directors may also benefit minority shareholders in East Asian corporations as they also have the potential to balance the powers of management and controlling shareholders with the interest of minority shareholders. However, in practice, the role and effectiveness of outside directors are questionable. In Thailand, for example, due to the ambiguous law on the responsibilities and authority of these directors, the roles of independent directors in monitoring management are unclear.²⁴³ The law is discussed in Chapter 4. Scholars point out that these outside directors are reluctant to intervene in the decisions of controlling shareholders as they consider controlling shareholders to be the owners of the companies.²⁴⁴ In the US, due to their large stake in corporations and experiences, institutional investors play an important role in monitoring management on behalf of small investors. However, institutional investors in East Asian corporations do not yet have the same potential. Compared with controlling shareholders, institutional shareholdings are relatively small so they do not have sufficient control rights to influence the management of these companies.²⁴⁵ In addition to these internal

²⁴² Young et al, above n 189, 200.

²⁴³ Netirata Auttavoothisilpa, *Protection of Minority Shareholders in Public Limited Companies* (M Laws Thesis, Ramkhamhaeng University, 1996) 108–10.

²⁴⁴ Deunden Nikomborirak and Somkiat Tangkitvanich, *Thai Corporate Governance: From Crisis to Recovery* (1999) <http://www.nomurafoundation.or.jp/data/19990129-30_Deunden_Nikomborirak_-_Somkiat_Tangkitvanich.pdf> at 20 March 2012 1; Deunden Nikomborirak, 'Problems of Corporate Governance Reform in Thailand' in Ferdinand A Gul and Tsui Judy SL (eds), *Governance of East Asian Corporations: Post Asian Financial Crisis* (2004) 226–7; Piman Limpaphayom and Thomas J Connelly, *Corporate governance in Thailand* (2004) Thai Institute of Directors Association <<http://ssrn.com/abstract=965300>> at 20 March 2012, 40.

²⁴⁵ For instance, in Thailand, the research found that the shares of turnover of securities transactions contributed by institutional investors during the first and second quarter of 1998 were only 5.80 and 6.42 per cent respectively. Nikomborirak, above n 244 [Problems of Corporate Governance Reform in Thailand], Table 11.3.

mechanisms, the two other external mechanisms operating in the US are the external market for managers and the market for corporation control. Although the benefits of these mechanisms are widely recognised in the US, they do not exist in East Asian countries. Because of the concentrated ownership structure of East Asian corporations, the controlling shareholders elect only trusted associates as members of the board of directors to protect their interests. Although these managers may perform poorly, the controlling shareholders are unlikely to remove them. Due to ownership concentration, it is not possible for a takeover to occur either, as large shareholders own a sufficient amount of shares to shield themselves and their managers from a takeover bid. In all, the mechanisms functioning to protect minority shareholders in the US context are not adapted to East Asian corporations with their concentrated ownership structure.

In Germany, there is almost no market in corporate control. Supervisory boards, workers' participation, and banks play a significant role in ensuring that the managers are monitored and the benefits of all stakeholders are considered. Because of the similar corporate structures of German and East Asian corporations, such thing may be suitable for East Asian countries. However, as the German corporate governance model has developed in Germany's specific economic, historical and social context, it is questionable whether it is possible to employ it in the Asian context. For instance, Chinese listed companies formally have a two-tier board structure, similar to the German model; however, it is clear that in its implementation in 'China [it] does not have the deep roots that it does in Germany, especially in relation to employee participation'.²⁴⁶ In Germany, banks have a strong influence on German corporations through their own shares, the shares owned by their investment companies, and deposited shares. They hold sufficient voting power to appoint some of the members of both supervisory and management boards. Bank officers hold positions on the supervisory boards of most non-financial firms in Germany. The German experience indicates that the banks are empowered not only to monitor the company but also to partly operate company business. It is possible that bank participation could improve the governance of East Asian companies. However, research reveals that Thai banks

²⁴⁶ Julian Roche, *Corporate Governance in Asia* (2004) 77; see also Jay Dahya, Yusuf Karbhari and Jason Zezong Xiao, 'The Supervisory Board in Chinese Listed Companies: Problems, Causes, Consequences and Remedies' in Malcolm Warner (ed), *The Future of Chinese Management* (2003) 118–137.

themselves do not have good corporate governance.²⁴⁷ The 1997 financial crisis revealed considerable malpractice in East Asian banks and a close connection between bankers and company insiders. Hence the banks may not be able to effectively monitor managers or counterbalance the power of controlling shareholders.

The analysis indicates that neither US nor German models may be suitable for the East Asian corporate structures and business practices. The development of both the US and German legal models have been based on their distinctive economic, historical, and political backgrounds. The reforms in both jurisdictions have been suited to their own local conditions.²⁴⁸ There are other reasons, found in comparative law studies, considered in Chapter 8 that mechanisms that work well in one country may work differently in another. It is therefore important to carefully assess whether, and how, Western models may be applied in East Asian contexts.

2.6 Conclusion

The corporate structures of East Asian corporations are similar to that of German corporations and significantly different from that of US firms. Shares of US firms are normally held by a large number of small shareholders and one shareholder is unlikely to control a corporation. The fundamental conflict to be resolved by good corporate governance is between the directors, the agents, and the shareholders, the principals. In German and Thai firms, which are in the hands of controlling shareholders, the conflicts of interests are between principals and principals, the controlling and the minority shareholders, rather than between principals and agents. There are serious questions whether the mechanisms developed and applied in the US can be employed in East Asian corporate law and regulatory systems to enhance protection for minority shareholders. While the shareholding patterns in German and East Asian firms are similar, German corporate governance may not be effective for East Asian corporations either. In the East Asian corporate governance concept, controlling shareholders are strong and the banks and markets are weak. Further research is required to determine how to effectively protect minority shareholders in this particular context. The next

²⁴⁷ Nikomborirak, above n 244 [Problems of Corporate Governance Reform in Thailand], 230.

²⁴⁸ These backgrounds are discussed in Sections 2.3 and 2.4.

chapter reviews the literature, the law and regulatory practices in Thailand on the economy, corporate governance, and business practices from the perspective of minority shareholders' protection.

Chapter 3

The Legal Framework of Minority Shareholders' Protection in Thailand

- 3.1 Introduction
- 3.2 Background
 - 3.2.1 Thai companies and company law
 - 3.2.2 Legal transplants in Thai company law
 - 3.2.2.1 The critique on legal transplants
 - 3.2.2.2 Four phases of legal transplants in Thai company law
 - 3.2.3 The Stock Exchange of Thailand
 - 3.2.3.1 The development of the Stock Exchange of Thailand
 - 3.2.3.2 Individual shareholders' role in the Thai capital market
- 3.3 Reforms to minority shareholders' protection in Thailand
 - 3.3.1 The demand for legal reform in Thailand
 - 3.3.1.1 Government-led policies
 - 3.3.1.2 Demand from the private sector
 - 3.3.2 Post-1997 crisis reform
 - 3.3.2.1 Institutions
 - 3.3.2.2 Code of Corporate Governance
- 3.4 Thai corporate and securities laws on protecting minority shareholders
 - 3.4.1 Corporate law
 - 3.4.2 Securities law
 - 3.4.3 Regulations of the Securities and Exchange Commission
 - 3.4.4 Regulations and Listing Rules of the Stock Exchange of Thailand
- 3.5 Securities regulator and law enforcement agencies
 - 3.5.1 The Securities and Exchange Commission
 - 3.5.1.1 Criticisms of the Securities and Exchange Commission
 - 3.5.2 Thai legal enforcement agencies
- 3.6 Conclusion

3.1 Introduction

The previous chapter gave an overview of the concept of minority shareholders' protection in the United States, German, and East Asian contexts. This chapter describes the contemporary Thai legal framework for minority shareholders' protection and its wider legal, political and economic contexts. The chapter, firstly, covers the development of Thai law and economy and the development of the Thai stock market. Secondly, it reviews the evolution of Thai company and securities laws and regulations

after the 1997 Asian financial crisis. Thirdly, it outlines the present Thai laws and regulations on minority shareholders' protection. It concludes with an overview of the Thai corporate and securities regulatory bodies.

3.2 Background

3.2.1 Thai companies and company law

The concept of the commercial corporation as a separate legal person is, itself, a concept transplanted into Thai law from Western European legal systems. The concept was carried into East Asia by two historically significant chartered companies. Major changes occurred in what is now Thailand at the end of the Burmo-Siamese War of 1765–1767.¹ It was a turning-point for the four-centuries-old Siamese kingdom. The new king, Taksin, reunited the country and, to rebuild its prosperity, promoted the country's relations with China, Britain and the Netherlands. The ruling elite amassed wealth through trade as well as through war. King Taksin also encouraged the migration of Chinese. Many became labourers in ports and towns. Some became farmers. Their significance in the economy increased as they became traders, shop keepers, factory owners, and in some cases, agents of the government as tax farmers raising royal revenue.² The political and social elite expanded their trading activities. There was, however, little friction between the Chinese and Thais in spite of potential competition in trade. Thai preferred to work for the Crown. Chinese established good relations with the Thai elites. Significant businesses became interlocking associations between families.³ Buddhist tolerance, shared by both, discouraged discrimination between them.⁴

European traders and the two great chartered East India Companies were able to engage in business as the king permitted. Unlike Chinese merchants, they could not trade freely

¹ For details of the Thai economy before the Bangkok period, see Chris Baker and Pasuk Phongpaichit, *A History of Thailand* (2005) Section 1.

² During the reign of King Rama IV of the Chakri dynasty, the number of Chinese tax farmers was over 250 while that of Thai tax farmers was only 51. See Akira Suehiro, *Capital Accumulation in Thailand 1855–1985* (1996).

³ Gordon Redding, *The Spirit of Chinese Capitalism* (1990) 31–2.

⁴ Baker and Phongpaichit, above n 1, 95.

and had to pay higher taxes. This ultimately led Britain to push for free trade which was granted in the Bowring Treaty of 1855. Under it, Western traders⁵ could freely engage in business activities. The businesses in which they mainly invested were importing and exporting, commercial banks, industrial enterprises, and other professional services.⁶

The first formal company under Thai law was created in 1889. An Italian engineer proposed to excavate a canal under a contract with the Thai government.⁷ Although the government wanted the canal built, it was reluctant to grant permission to the engineer as, because of the extraterritorial rights given to foreigners under the unequal treaties, he would not be subject to Thai law or Thai courts. The government established a Thai company and then entered into a contract with it so that the enterprise and the contract were subject to Thai law. In the absence of regulations relating to companies, it was created as a chartered company following the example of European chartered companies. After its establishment, a number of merchants applied for the king's approval to set up companies. The government realised the benefit of this business form and then enacted the Partnership and Company Act of 1911. Companies then could be freely established. However, for specific businesses, such as banking, insurance, and transportation, the king's approval was still required.⁸ In 1928 a more complete company law was enacted in the Civil and Commercial Code. This is discussed later in the context of transplanting corporate law in Thailand.

The first major reform of Thai company law occurred because of the economic growth that took place in the 1970s. Thailand became a major site for Japanese offshoring manufacture after 1973.⁹ To promote economic development, the Thai government enacted the Public Companies Act of 1978 to expand capital raising. However, given the restrictions on share allocation, in the 14 years after the Act had come into effect, only 33 public companies were registered. In the 1980s the Thai economy reached

⁵ Principally American, British, French, and German.

⁶ Suehiro, above n 2, 42–3.

⁷ Tipchanok Ratanosoth, *Partnership and Company Laws* (2010) 186–7.

⁸ Partnership and Company Act B.E. 2454 (1911) (Thailand) s 115.

⁹ Pasuk Phongpaichit and Chris Baker, *Thailand's Crisis* (2000), 18. In addition, the revaluation of the yen and other Asian currencies spurred economic growth in Thailand. In 1982 100 Thai baht was approximately 1180 yen but depreciated to 508 yen in 1988. Japanese industries are therefore said to have shifted from Japan to Thailand. See Pasuk Phongpaichit and Chris Baker, *Thailand's Boom and Bust* (1998) 69–70.

another turning point. Under the influence of the World Bank, Thai technocrats began to move Thailand towards an export-led economy¹⁰ in the belief that further liberalisation would provide greater opportunities for investment and trade and promote greater economic development.¹¹ A boom commenced in 1990 after the Thai government deregulated the financial system and some restricted industries.¹² Economic growth has accelerated since. The Public Companies Act of 1978 was repealed by the Public Companies Act of 1992 to facilitate fund raising. In addition, the Securities and Exchange Act of 1992 was enacted to expand capital market trading.

The final stage of company law reform came after the 1997 financial crisis.¹³ The economic boom ended in mid-1996.¹⁴ The stock market and real estate market started to fall. Foreign investors began to pull out their loans. A year later, the bursting of the bubble reached its final stage. Finance One, one of Thailand's most successful financial companies, collapsed under a large number of non-performing loans.¹⁵ The Bank of

¹⁰ Ibid 70.

¹¹ Snoh Unakul, the leader of the Thai planning board in the 1980s, mentioned:

Thailand will rank among the forefront countries capable of adjusting and performing strongly. The current trade is useful for Thailand, as it will open up opportunities for investment and trade. More countries will pay attention to the region and us. ... What needs to be done is to continue our restructuring. ... *The government must change from controlling to promoting and supporting.* ... *What is necessary in terms of investment must be left to the private sector.* ... We must adjust the country to export orientation. ... Bangkok will become a centre for business and air transport. (Emphasis added)

See Phongpachit and Baker, above n 9, 23.

¹² Baker and Phongpaichit, above n 1, 203–4. In 1990, Thailand accepted the obligation under Article VIII of the International Monetary Fund that required the removal of government control over all foreign-exchange transactions. In 1993, the Bangkok International Banking Facility (BIBF) was set up to make Bangkok a centre of financial services. The BIBF allowed local and foreign commercial banks to take deposits or borrow in foreign currencies from abroad and lend them in Thailand and other countries in the region. By December 1995 BIBF provided licences to 15 domestic banks and 30 foreign banks. Jonathan E Leightner, 'Globalization and Thailand's Financial Crisis' (1999) 33(2) *Journal of Economic Issues* 367, 368. In addition to financial liberalisation, the critical factor that accelerated the capital inflows was the interest rate in Thailand that was significantly higher than world interest rates. Thai entrepreneurs therefore preferred borrowing money from abroad as the interest rate was lower. Besides, the risk of currency exchange was fixed as the Thai government employed the pegged exchange rate at 25 baht to US\$.

¹³ For a general study on the reform in legal and corporate governance after the 1997 financial crisis, see Chris Dixon, 'Post-Crisis Restructuring: Foreign Ownership, Corporate Resistance and Economic Nationalism in Thailand' (2004) 26(1) *Contemporary Southeast Asia: A Journal of International & Strategic Affairs* 45.

¹⁴ See Ammar Siamwalla, 'Picking up the Pieces: Bank and Corporate Restructuring in post-1997 Thailand' (Paper presented at the Financial and Corporate Sectors Restructuring in East and South-East Asia, Seoul, Korea, 30 May–1 June 2001) 18–20.

¹⁵ It was considered as, among Thai small- and medium-sized banks, the largest financial company in Thailand with assets of US\$4 billion. Leightner, above n 12, 369.

Thailand, the central bank, and financial regulator, ordered 58 financial companies to cease trading.¹⁶ The number of non-performing loans increased dramatically.¹⁷ Despite the economic downturn, the government refused to permit the baht to depreciate.¹⁸ Currency speculators attacked the baht. The Thai government used foreign currency reserves to peg the baht with the US dollar.¹⁹ This defensive strategy failed and the government was forced to float the baht on 2 July 1997.²⁰ Consequently, the currency lost 50 per cent of its value. This placed serious burdens on companies required to repay their loans in foreign currencies. Without sufficient reserves, the Bank of Thailand called on the International Monetary Fund (IMF) for help. In exchange for its financial support package, Thai domestic financial policy was effectively handed over to the control of the IMF. One of its requirements was to reform Thai company and securities laws. It required Thailand to adopt the standards of the Organisation for Economic Co-operation and Development (OECD) to improve corporate governance in Thai companies.

As can be seen from the foregoing account, the main factor producing changes in Thai company law has been the development of the Thai economy. This finding accords with Milhaupt and Pistor's thesis on the rolling relationship between legal and economic development.²¹ From the beginning, companies and company law have existed to facilitate business. Economic growth has also led to changes in Thai company law to advance to a new form of investment and capital accumulation – the publicly listed

¹⁶ After the suspension, the management of these finance companies were required to submit rehabilitation plans; however, there were only two from 58 companies authorised to continue their businesses. The assets of the 56 financial companies were transferred to the Financial Restructuring Authority (FIDF), financially supported by the Bank of Thailand. Later, the assets were auctioned off and could be recovered at approximately 25 per cent of their face value. Ammar Siamwalla, 'Anatomy of the Thai Economic Crisis' in Peter Warr (ed), *Thailand Beyond the Crisis* (2005) 70–72.

¹⁷ Phongpaichit and Baker (1998), above n 9, 104.

¹⁸ With the intention of stabilising the value of the Thai currency, the Thai government employed a fixed exchange rate system. Under this system, the central bank had to ensure that the amount of foreign reserves was sufficient to ensure that it could supply the market with foreign currency. Thailand had maintained the exchange rate of 25 baht to US\$ for 13 years. Siamwalla, a leading Thai scholar, argued that one of the causations of the financial crisis in 1997 was the use of a fixed exchange-rate scheme. Siamwalla, above n 16, 68–9.

¹⁹ It is reported that the net international reserves decreased from US\$23.6 billion in April 1997 to US\$2.9 billion in June 1997. Sukanda Lewis, 'Banking System and Capital Market Development: The Case of Thailand' (1998) 35(1&2 June/December) *Malaysian Journal of Economic Studies* 95, 95.

²⁰ Phongpaichit and Baker reported that the central bank had committed US\$23.4 billion in the battle of the reserves. See Phongpaichit and Baker (1998), above n 9, 124.

²¹ Curtis J Milhaupt and Katharina Pistor, *Law and Capitalism: What Corporate Crises Reveal about Legal Systems and Economic Development around the World* (2008).

company. Similarly, economic failure has also led to legal reforms to regulate companies and to prevent the recurrence of scandals and crises.

3.2.2 Legal transplants in Thai company law

The above section provides a general background to Thai company and Thai company law. The following sections aim to examine legal transplants in Thai company law by considering how Thai company law has been transplanted. In addition, the factors driving such transplants are considered.

3.2.2.1 The critique on legal transplants

The interest in what may now be called legal transplants began with Montesquieu's concern over transplants from Roman law into French law and his belief that the French would have more liberty under Frankish rather than Roman legal institutions.²² Montesquieu claimed that there was a complex link between law and its environment. The spirit of a people was influenced by 'various causes: by the climate, by the religion, by the laws, by the maxims of government, by precedents, morals, and customs'.²³ These factors also determined the spirit of the law in each country. Given their different circumstances, he claimed that it was unusual for the laws of one country to be appropriate for another. The academic study of legal transplants was further stimulated by two French scholars, Lambert and Saleilles, who founded the International Congress for Comparative Law in 1900.²⁴ Legal transplants since then have been one of the central issues in comparative law study. It received a more attention after 1970 when one of the Congress's sessions was dedicated to the Global Reception of Foreign Law. Four years later, Watson's publications made the study of legal transplants a major theme of comparative law study.

²² Baron De Montesquieu, *The Spirit of Laws* (Thomas Nugent trans, 1914) 316.

²³ Ibid.

²⁴ Konrad Zweigert and Hein Kötz, *Introduction to Comparative Law* (Tony Weir trans, 3rd revised ed, 1998).

Watson believed that legal transplants were common in practice. He claimed:

In the most places at most times borrowing is the most fruitful source of legal change. The borrowing may be from within the system, by analogy – from negligence in torts to negligence in contract, for instance – or from another legal system. The act of borrowing is usually *simple*.²⁵ (Emphasis added)

Many Western countries, as the work of Montesquieu indicated, developed their legal systems through borrowing laws from other jurisdictions.²⁶ Watson argued that law developed from the wishes of lawmakers who believed that a foreign law would be beneficial when transplanted into their society rather than emerging as an original idea from social structures.²⁷ He argued that a legal transplant might be very successful even though the relevant social, economic, and political circumstances of the donor and recipient systems were significantly different.²⁸ He explained:

What, in my opinion, the law reformer should be after in looking at foreign systems was an idea which could be transformed into part of the law of his country. For this a systematic knowledge of the law or political structure of the donor system was not necessary, though a law reformer with such knowledge would be more efficient. Successful borrowing could be achieved even when nothing was known of the political, social or economic context of the foreign law.²⁹

Other scholars, however, argued that law was not autonomous from the society in which it operated. Legal rules could not be easily transplanted from one legal system to another as they were deeply attached to the social structure. This was Montesquieu's view and was followed by a number of scholars, including Legrand and Kahn-Freund. Legrand saw legal transplants as impossible. He argued:

No rule in the borrowing jurisdiction can have any significance as regards the rule in the jurisdiction from which it is borrowed. This is because, as it crosses boundaries, the original rule necessarily undergoes a change that affects it *qua* rule. ... The fact that

²⁵ Alan Watson, 'Aspects of Reception of Law' (1996) 44 *American Journal of Comparative Law* 335, 335; See Edward M Wise, 'The Transplant of Legal Patterns' (1990) 38 *American Journal of Comparative Law* 1.

²⁶ See Alan Watson, *Legal Transplants: An Approach to Comparative Law* (1974); Alan Watson, 'From Legal Transplants to Legal Formants' (1995) 43 *American Journal of Comparative Law* 469.

²⁷ Alan Watson, 'Comparative Law and Legal Change' (1978) 37 *Cambridge Law Journal* 313, 315.

²⁸ Alan Watson, 'Legal Transplants and Law Reform' (1976) 92 *Law Quarterly Review* 79, 80.

²⁹ *Ibid* 79.

exactly the same word gets printed or uttered again and again does not mean that exactly the same meaning (which is half the word) spreads from minds to minds.³⁰

To him, law had a close connection with its original culture as it 'derives from historical experience'.³¹ A rule therefore could not be seen simply as a rule.³² The meaning of a rule did not appear in the word expressing such a rule but in its wider contexts. The invested meaning in the adopted rule is culture-specific, and without the similar crucial element in donor and recipient countries, it does not survive the journey from one place to another.³³ In other words, when the words transfer to another jurisdiction the meaning of such words is changed. There are no two legal systems exactly alike. Similarly, Kahn-Freund suggested that transplanting the law of one jurisdiction into another entails the risk of rejection.³⁴ He argued: '[t]he use of comparative law for practical purposes becomes an abuse only if it is informed by a legalistic spirit which ignores [the] context of law'.³⁵ Influenced by Kahn-Freund, Teubner adopted a position between Watson and Legrand. Teubner considered the transferred rule as an irritation in the legal system to which it is transferred rather than a transplant. He places law in the context of systems that are coupled or systematically linked into aspects of the economic, social and political systems. He explained the consequence of the coupling:

Legal irritants cannot be domesticated; they are not transformed from something alien into something familiar, not adapted to a new cultural context, rather they will unleash an evolutionary dynamic in which the external rules' meaning will be reconstructed and the internal context will undergo fundamental change.³⁶

Teubner divided laws into two categories based on the degree of their connection to social contexts: those that were loosely coupled and those that were tightly coupled with 'social processes'.³⁷ While the former tended to be comparably easy to transfer,³⁸ there

³⁰ Pierre Legrand, 'The Impossibility of "Legal Transplants"' (1997) 4 *Maastricht Journal of European and Comparative Law* 111, 120.

³¹ Pierre Legrand, 'European Legal Systems Are Not Converging' (1996) 45 *International and Comparative Law Quarterly* 52, 56–7; see also Pierre Legrand, 'Against a European Civil Code' (1997) 60 *Modern Law Review* 44.

³² *Ibid.*

³³ Pierre Legrand, 'What "Legal Transplants"?' in David Nelken and Johannes Feest (eds), *Adapting Legal Cultures* (2001) 60.

³⁴ Otto Kahn-Freund, 'On Uses and Misuses of Comparative Law' (1974) 37(1) *The Modern Law Review* 1, 27.

³⁵ *Ibid.* 27.

³⁶ Gunther Teubner, 'Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences' (1998) 61 *Modern Law Review* 11, 12.

³⁷ *Ibid.* 18–20.

³⁸ Teubner however pointed out:

was resistance to the transfer of the latter.³⁹ The resistance was not only from the existing legal system but also from the context in which such a system operated, including politics, economy, technology, and culture.⁴⁰ The transferred rule would irritate both the legal system and these other systems in the recipient jurisdiction.⁴¹ The effect on both would be evolutionary on the national law or cause ‘a simultaneous and complementary change in the other social fields’.⁴²

Similarly to Teubner, Berkowitz *et al* pointed out that a foreign law would be modified after adoption.⁴³ The adaptation was done by local legal practices or conditions in order to put the transplanted rules in an appropriate position in the legal system.⁴⁴ The change was made to implement these rules in practice.⁴⁵ To make the modification effective, the key factor is the local agents. As suggested by Berkowitz *et al*, a legal transplant was likely to work if the local agents were already familiar with the basic principles of foreign legal doctrines.⁴⁶ They further argued that “the demand for law” was important in the success.⁴⁷ They explained:

Our argument is that for law to be effective, a demand for law must exist so that the law on the books will actually be used in practice and legal intermediaries responsible for developing the law are responsive to this demand. If the transplant adapted the law to local conditions ... then we would expect that the law would be used. Because the law would be used, a strong public demand for institutions to enforce this law would follow. And, legal intermediaries that are responsible for developing and enforcing this imported law would be able to develop the law so as to match demand, because the

Even in those situations where the law is rather ‘technical’, insulated from its social context, legal transfer is not smooth and simple but has to be assimilated to the deep structure of the new law, to the social world constructions that are unique to the different legal culture.

Ibid 19.

³⁹ Ibid 18–19.

⁴⁰ Ibid 22–24.

⁴¹ Ibid 31–2.

⁴² Ibid 22.

⁴³ Daniel Berkowitz, Katharina Pistor and Jean-Francois Richard, ‘Economic Development, Legality, and the Transplant Effect’ (2003) 47 *European Economic Review* 165, 174.

⁴⁴ Ibid.

⁴⁵ Ibid 174–5.

⁴⁶ Daniel Berkowitz, Katharina Pistor and Jean-Francois Richard, ‘The Transplant Effect’ (2003) 51 *American Journal of Comparative Law* 163, 189.

⁴⁷ See Curtis J Milhaupt, ‘Beyond Legal Origin: Rethinking Law’s Relationship to the Economy – Implications for Policy’ (2009) 57 *American Journal of Comparative Law* 831. Kahn-Freund also acknowledged the roles of local interest groups in influencing the legal adoption through the law-making and the decision-making process. Kahn-Freund, above n 34, 12–3.

strong demand for law would provide resources for legal change. Where these conditions are present we would expect that the legal order to function just as effectively as in an origin country where the law was developed internally. However, if the law was not adapted to local conditions, or if it was imposed via colonization and the population within the transplant was not familiar with the law, then we would expect that this initial demand for using these laws to be weak. ... Countries that receive the law in this fashion are thus subject to the “transplant effect”: their legal order would function less effectively than origins or transplants that either adapted the law to local conditions and/or had a population that was familiar with the transplanted law.⁴⁸

There is also a debate on the ability of transplanted law to adapt to the environment of the recipient jurisdiction especially in fast-changing circumstances. Some scholars argue that the common law is better able to respond to incremental changes. This was because of the constant developments made possible by case law which is more adaptive to changing social and economical requirements.⁴⁹ Siems however disagrees. He studied how laws on shareholders’ protection had developed from 1995 to 2005 in a number of recipient countries. The study found that there were a number of factors relating to adaptability including the political system, legislative process, the courts, and the relationships between the donor and recipient jurisdictions.⁵⁰ The degree of legal adaptation is therefore not solely based on legal families. Berkowitz *et al* also support this view. They claim that the way in which law is transplanted is more important than its origin.⁵¹ Voluntary transplantations encourage the recipient jurisdiction to make more significant adaptations to the borrowed law.

As the earlier literature referred to shows, there is no consensus on whether legal transplants are possible. The arguments are not only based on legal issues but extend to economic, historic, and political factors. The earlier debates generally focused on the feasibility of legal transplants. They have moved to focus on the effects and the conditions for the success or failure of legal transplants.

⁴⁸ Berkowitz, Pistor and Richard, above n 46, 167–8.

⁴⁹ Ralf Michaels, 'Comparative Law by Numbers? Legal Origins Thesis, *Doing Business* Reports, and the Silence of Traditional Comparative Law' (2009) 57 *American Journal of Comparative Law* 765, 769.

⁵⁰ Mathias M Siems, 'Shareholder Protection around the World: "Leximetric II' (2008) 33 *Delaware Journal of Corporate Law* 111, 141-2. See also Mathias M Siems, 'Legal Adaptability in Elbonia' (2006) 4 *International Journal of Law in Context* 393.

⁵¹ Berkowitz, Pistor and Richard, above n 46, 190.

3.2.2.2 Four phases of legal transplants in Thai company law

Legal transplantation in Thai company law can be divided into four phases – prior to 1923, 1923, 1992 and 2008. The year 1923 is used to separate the first and second phases as in that year the Civil and Commercial Code was published. This was the foundation of Thai company law. In 1992 both the Public Limited Company Act (“PLC Act”) and Securities and Exchange Act (“Securities Act”) were significantly amended. The final phase was in 2008 when a large number of legal concepts seeking to protect minority shareholders were introduced.

Traditional Thai law only recognised the concept of partnership. The first written law appeared in the early 16th century.⁵² This law was later acknowledged in the Three Seals Law or *Kotmai Tra Sam Duang*.⁵³ The Three Seals Law was promulgated in 1805 by the first king of the Chakri dynasty and is considered to be a corpus of Thai traditional laws.⁵⁴ The Three Seals Law, however, did not specify the characteristic of partnership or the rights and obligations of partners.⁵⁵ It contained only two relevant provisions. The first provision merely required the parties to share profits and losses. The second provision specified how the assets were to be distributed among partners during war.

The concept of a company was first adopted in 1889. As discussed earlier, this occurred as the Thai government desired to enter into a contract with an Italian engineer to excavate a canal.⁵⁶ However, the government was reluctant to do so as, under the extraterritorial rights granted by the Bowring Treaty of 1855, he would not be subject to Thai law or Thai courts. The government, therefore, used the corporate form to create a legal person subject to Thai law. To establish a company, a charter from the king was required. In practice, many Thai legal practitioners were not familiar with the separate legal personality of a company. They believed that the managers were a part of the

⁵² Sunee Mullikaman et al, 'Revolution of Thai Law in Two Centuries' (Chulalongkorn University, 1982) 152.

⁵³ Ibid.

⁵⁴ Yoneo Ishiii, *Computerization of the Thammasat Version of the Kotmai Tra Sam Duang* (2005) Chulachomklao Royal Military Academy <http://adap.crma.ac.th/KotmaiTraSamDuang/explanation_en.html> at 20 March 2012.

⁵⁵ Mullikaman, above n 52, 152.

⁵⁶ Ratanosoth, above n 7, 186–7.

company and *vice versa*. The success of chartered companies and the demands of merchants to establish companies led to the government allowing companies to be freely established under the Partnership and Company Act of 1911.⁵⁷ The Act drew on the rules applied by, and the decisions of, the Thai courts. The courts' decisions were greatly influenced by English company law. This was because Thai judges had been mainly educated in Britain.

The second phase of transplants occurred in 1923.⁵⁸ To understand this phase, it is necessary to understand the wider factors driving transplantation of law in Thailand. During the 16th century, like other South Asian countries, Thailand was under the threat of British and French annexation.⁵⁹ According to European states, Thai law, especially criminal law and criminal procedure, was archaic and irrational. The principles of equality before the law or no penalty without a law (*nulla poena sine lege*) were not applied. Physical punishments were severe, although some were still to be found in the Western legal systems of the period. In addition to the death penalty, there were other punishments including cutting off hands and feet, flogging, and tattooing on the face. Periods of imprisonment were not specified. The king could order any punishment he pleased. The criminal procedure assumed that an accused was guilty and bore the onus of proving innocence. Many European countries tried to negotiate for extraterritorial rights so that all conflicts between their citizens and Thai subjects would be decided in their courts under their law. The first country to successfully conclude such a treaty was Britain, by Sir John Bowring, in 1855. Eventually, Thailand entered into similar treaties with another 13 nations.⁶⁰

While neighbouring countries were annexed by Britain and France, Thailand secured its sovereignty by avoiding a pretext for annexation in the conflict between Britain and France over which should annex it and in developing political and legal institutions

⁵⁷ Partnership and Company Act B.E. 2454 (1911) (Thailand) s 115. However, some businesses, including banking, insurance, and transportation, remained restricted.

⁵⁸ See Charnchai Sawengsak, *Influence of France in Thai Legal Reformation* (1996); Swang Boonchalermvipast, 'The Thai Legal History' in Prachoom Chomchai (ed), *Development of Legal Systems in Asia: Experiences of Japan and Thailand* (1997); Kittisak Prokati, *Thai Legal Reform under European Influence* (2006); Swang Boonchalermvipast, *Thai Legal History* (2009).

⁵⁹ See *Diplomatic History of Thailand: Extraterritoriality* (2010) Ministry of Foreign Affairs <<http://www.mfa.go.th/main/en/organize/1085/19295-Extraterritoriality.html>> at 20 March 2012.

⁶⁰ Boonchalermvipast, above n 58 [Thai Legal History], 137.

which would be respected by Western powers. The Thai government reformed the criminal law and criminal procedure, and the judicial system by adopting Western legal concepts, including principles of equality before the law and civil rights. This not only weakened claims by Western powers for extraterritoriality but also improved the Thai legal system.⁶¹ At the beginning of these legal reforms, a decision had to be made on whether Thailand would adopt a civil or common law system. Prince Rapee,⁶² who graduated in law from Oxford University and became minister of justice, preferred common law, as he believed codifying was time-consuming and costly. He also pointed out that codes limited legal application and interpretation. Also, many Thai lawyers and judges had graduated from common law countries and were familiar with the common law system. However, King Rama V decided on a system of codification. The main reason was that under pressure of annexation, Thailand could not wait for the courts to develop case law.⁶³ As well, codification made Thai law more systematic.

The drafting of the Civil and Commercial Code commenced in 1908. French influence was significant. All of the members of the first drafting committee were French and the Civil Code of France was employed as a model. The Code was drafted in English and then translated into Thai by the translating committee.⁶⁴ It took 15 years for three drafting committees to finish drafting the first two books, general principles and obligations. However, after these were promulgated in 1923, Thai judges and lawyers claimed that they did not understand the language used. Finally, a fourth *ad hoc* committee, consisting of three Thais and one French lawyer, was authorised to amend the two books and draft the remaining books. The committee considered the civil codes of France, Italy, Spain, Chile, Portugal, Sweden, Japan, and Germany as a possible model.⁶⁵ It eventually chose the German Civil Code (*Bürgerliches Gesetzbuch*).⁶⁶ It was considered more up to date than the French Civil Code. The decision was also

⁶¹ Chachapon Jayaphorn, 'Reforming of the Thai Legal System at the Beginning of the 20th Century: Context and Origin' (2005) <<http://www.thailawforum.com/articles/reformation1.html#1>> at 20 March 2012.

⁶² One of Rama V's sons.

⁶³ Chuathai mentioned that the codification in Thailand brought a significant change to Thai legal history. The English common law system had been employed in Thailand for half a decade. Such change, therefore, had an impact on not only the laws on books but also the legal system as a whole. Somyot Chuathai, *Civil and Commercial Code* (2008) 11–2.

⁶⁴ Tamara Lynn Loos, *Subject Siam: Family, Law, and Colonial Modernity in Thailand* (2005) 62.

⁶⁵ Ibid 66.

⁶⁶ Ibid.

influenced by the experience of Japan in using it to create its Civil Code (*Minpō*). To maintain good relations with France, however, some provisions in the first two books were retained. The amendments became effective in 1925. The third book was promulgated in 1928 and revised in 1929.

Company law was incorporated into the third book of the Civil and Commercial Code. The provisions in the Code were similar to those in the Partnership and Company Act of 1911 but a number were revised. The significant change was the provisions on directors' duties. The Partnership and Company Act merely stated that a company was responsible to the third party for any damage.⁶⁷ The law did not otherwise define the scope of directors' duties. The Civil and Commercial Code imposed on directors the duty of care and the duty of loyalty to the company.⁶⁸ These additional legal rules may reflect the continuing strong influence of English law and common law method. As mentioned, the existing Thai rules were not sufficient for complex commercial transactions; Thai courts had applied common law rules on a case-by-case basis. As Thai legal practitioners in the 1920s were familiar with English legal principle in this area, the drafting committee decided to adopt English company law in the Code.⁶⁹

The third phase of transplants was in 1992. As indicated earlier, the Thai economy grew significantly in the late 1980s. The Thai government liberalised many sectors. The financial system and some previously restricted industries were deregulated. To further promote economic growth, the Thai government also sought to develop the capital market. It revised both the Securities and PLC Acts in order to support that growth. A detailed discussion of the development of the Securities and PLC Acts is later in this chapter. Those revisions made a significant change to Thai company law. A number of provisions were incorporated to fill gaps in the previous provisions. For instance, the directors' duty of care had previously been stated as "the diligence of a careful businessman". The revised PLC Act required the directors to perform their duties "in good faith" and "in the interest of the company". The additional terms recognised these

⁶⁷ Partnership and Company Act B.E. 2454 (1911) (Thailand) s 169.

⁶⁸ Civil and Commercial Code B.E. 2468 (1925) (Thailand) s 1168.

⁶⁹ Tanin Kraivixien, 'Influence of English Laws in the Thai Legal System' (1974) 11(2) *The Chulalongkorn Law Journal* 1.

legal ideas in Thai law. Minority shareholders were also better protected. For instance, in merger transactions, the PLC Act required the company to offer to buy shares from dissenting shareholders at the market price. This had not been previously required. In addition, the revised Securities Act established the Securities and Exchange Commission as a single unified securities regulator. This was an adaptation of the model of the US Securities and Exchange Commission.

The fourth phase of transplants occurred in 2008. This can be seen as a significant change in Thai company and securities laws. As indicated earlier, the main purpose of the transplants was the pressure on the government from international institutions and its demand to improve Thai company and securities laws in order to attract both foreign and local investors. The Securities Act was considerably amended. A number of provisions were incorporated to provide better protection for minority shareholders. This included the right to propose agenda items at a shareholders' meeting⁷⁰ and the right to reimbursement of litigation costs of derivative actions.⁷¹ The law also imposed duties on auditors to monitor the management and report any suspicious transactions to the securities regulator.⁷² Directors' duties were also significantly revised in the latest Securities Act. The law further clarified the scope of the duty of care and introduced the legislative form of the business judgment rule.⁷³ The duty of loyalty was also significantly amended. As discussed in Chapter 5, legislators further particularised the duty of loyalty in the absence of judicial interpretation.

Over all, transplants in Thai company law have been driven by economic and political factors and the political elites.⁷⁴ The Thai government decided to adopt the concept of a separate legal entity to facilitate a major canal excavation and place it under Thai law. To further facilitate the use of the corporate form by Thai business people, the Thai

⁷⁰ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/28.

⁷¹ Ibid s 89/18.

⁷² Ibid s 89/25.

⁷³ Ibid s 89/8.

⁷⁴ Pistor studied the evolution of corporate law in 10 jurisdictions and found similar results. The research found that:

One of the most important lessons that can be drawn from [the paper] is that corporate law does not evolve in isolation, but in close interaction with socioeconomic conditions and politics, as well as other parts of the legal system.

Katharina Pistor et al, 'Evolution of Corporate Law: A Cross Country Comparison' (2002) 23 *University of Pennsylvania Journal of International Economic Law* 791, 864.

government promulgated the Partnership and Company Act of 1911. Later, under political pressure, the government decided to follow a system of civil law codification to regain extraterritorial rights. Since 1992, transplants have been part of economic development policies. This is also seen in the 2008 reforms which were also made under international pressure.

3.2.3 The Stock Exchange of Thailand

The following sections provide an understanding of the development of the Thai stock market to place Thai listed companies in the capital market. The roles of individual investors in the market are then discussed so that the place of minority shareholders in those markets is understood.

3.2.3.1 The development of the Stock Exchange of Thailand

The development of the modern Thai capital market falls into two phases.⁷⁵ The first period began in 1962. A group of private investors set up a stock exchange market in the form of a limited partnership. In 1963 it changed its status to that of a limited company, the “Bangkok Stock Exchange Co., Ltd”. The market was relatively small and inactive. Trading volumes were continually falling from 160 million baht per year in 1968 to only 26 million baht by the early 1970s.⁷⁶ The stock exchange eventually closed. The failure of the first capital market resulted from both a lack of government support and the investors’ limited understanding of stocks trading.⁷⁷ The second period started in the 1970s. The Second National Economic and Social Plan (1967–1971) revealed the government’s appreciation of the need for a national capital market.⁷⁸

⁷⁵ For details on the early stage of the development of the Thai stock exchange, see Sukri Kaocharern, 'The Development of the Securities Exchange in Thailand' (1976) 12(1) *International Journal of Accounting* 19.

⁷⁶ *History & Roles* (2009) The Stock Exchange of Thailand <http://www.set.or.th/en/about/overview/history_p1.html> at 20 March 2012.

⁷⁷ Prasarn Trairatvorakul, *The Necessity and Policy Guidelines to Develop the Thai Capital Market* (2002–2003) 25.

⁷⁸ Back to the 1960s, Thailand implemented the First National Economic and Social Development Plan (1961–1966) to promote sustainable economic growth and improve the standard of living of Thai people. See the First National Economic and Social Development Plan (1961–1966) Chapter 1 at <http://www.nesdb.go.th/Default.aspx?tabid=83>; the Second National Economic and Social Development Plan (1967–1971) Chapter 5 at <http://www.nesdb.go.th/Default.aspx?tabid=84>.

Following a recommendation made by Robbins,⁷⁹ the former chief economist of the US Securities and Exchange Commission (“SEC”), a government-supported equity market was established in April 1975 under the name of the “Securities Exchange of Thailand”. Later, in January 1991 its name was changed to the “Stock Exchange of Thailand”. A significant change in the Thai stock market came after the enactment of the Securities and Exchange Act of 1992 (“Securities Act”) that granted the exchange a monopoly.⁸⁰ The Act also established the Securities and Exchange Commission (“Thai SEC”) as a single unified supervisory agency to regulate the market.⁸¹ Under the Act, the board of directors and managers of the Stock Exchange of Thailand (“SET”) operate the market under the policies and regulations issued by the Thai SEC.⁸²

Although the Thai capital market has been established for almost 40 years, its role in the Thai economy remains slight. From 1988–1998 the amount of capital raised through the capital market accounted for only 11.06 per cent of Gross Fixed Capital Formation (GFCF). In the US, the United Kingdom, Japan, South Korea, and Singapore, the capital generated via the stock markets was around 54.4, 43.6, 14.6, 25.2 and 17.5 per cent of GFCF respectively.⁸³ In Thailand, bank loans amount to approximately 34.8 per cent of GFCF. In the US, the UK, Japan, South Korea, and Singapore, this is 14.1, 0.05, 12.6, 24.1 and 32.5 per cent of GFCF respectively.⁸⁴ In other words, the capital generated through the capital market accounts for only about 31.79 per cent of total bank loans. Compared with other Asian stock markets, the market capitalisation of the Thai stock exchange is also relatively small as shown in Table 3.1 below.

⁷⁹ The services of Robbins were suggested to Thailand by the World Bank. For his report on the development of the Thai capital market, see Sidney M Robbins, *A Capital Market in Thailand* (1970).

⁸⁰ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 155–6.

⁸¹ *Ibid* s 14.

⁸² *Ibid* s 167.

⁸³ Securities and Exchange Commission, 'The Roles of the Thai Stock Market in Fund Raising' (Securities and Exchange Commission, November 2000) 3.

⁸⁴ *Ibid*.

Table 3.1 Domestic market capitalisation of Asian Pacific stock markets (2008–2011)

(\$US billions)

Markets	January 2011	End 2010	End 2009	End 2008
Bursa Malaysia	412,912.9	408,689.1	289,219.4	189,232.2
Colombo SE	21,490.9	19,923.9	9,546.7	4,285.9
Hong Kong Exchange	2,723,751.9	2,711,316.2	2,305,142.8	1,328,768.5
Indonesia SE	333,084.1	360,388.1	214,941.5	98,760.6
Korea Exchange	1,122,170.8	1,091,911.5	834,596.9	470,797.7
Philippine SE	156,807.9	157,320.5	86,349.4	52,030.6
Shanghai SE	2,724,037.1	2,716,470.2	2,704,778.5	1,425,354.0
Shenzhen SE	1,233,101.4	1,311,370.1	868,374.0	353,430.0
Singapore Exchange	646,726.2	647,226.4	481,246.7	264,974.4
Taiwan SE Corp	836,530.8	818,490.5	658,991.4	356,710.6
Thailand SE	254,051.6	277,731.7	176,956.1	103,128.2
Tokyo SE Group	3,841,553.9	3,827,774.2	3,306,082.0	3,115,803.7

Source: World Federation Exchange (2012)

Trairatvorakul, a former secretary of the Thai SEC, pointed out that the Thai entrepreneurs prefers obtaining capital from a financial institution rather than from the stock market as listing a company dilutes the entrepreneurs' power over the company.⁸⁵ As well, under the listing rules, listed companies must comply with disclosure requirements. Entrepreneurs may be reluctant to list on the market as they prefer to keep information within the family.⁸⁶

The Thai government has attempted to enlarge the market size in different ways. Firstly, it encourages companies to list on the market.⁸⁷ Secondly, it sets up another capital market for small and medium-sized enterprises, known as the Market for Alternative Investment (MAI).⁸⁸ Thirdly, the government, through the SET has expanded the range of securities products from stocks to bonds, futures, options, and options on futures. In 2003, the Bond Electronic Exchange (BEX) was officially launched with the aim of

⁸⁵ Trairatvorakul, above n 77, 41.

⁸⁶ Michael Beckman, *The Asian Insider: Unconventional Wisdom for Asian Business* (2004) 68–9.

⁸⁷ For instance, the Thai SEC initiated a project to encourage potential businesses around Thailand to list on the market. See, Securities and Exchange Commission, *New Stock, Proud of Province* (2012) <http://www.sec.or.th/IPO/Content_IPO.jsp?categoryID=CAT0000689&lang=th> at 20 March 2012.

⁸⁸ A company with paid-up capital of over 200 million baht is able to list on the Thai stock market while a company with paid-up capital of over 40 million baht lists on the MAI. *Listing Information* (2012) Stock Exchange of Thailand <http://www.set.or.th/th/products/listing/criteria_p5.html> at 20 March 2012.

developing Thailand's secondary bond market.⁸⁹ The Thailand Futures Exchange Plc (TFEX) was established in 2004 for trading and hedging of derivative products such as gold, oil, and foreign currencies.

In all, the development of the Thai stock market has been mainly driven by the government. However, its role in the Thai economy has not been evident. As the issue focused on in this research is minority shareholders, the research further examines the role of minority shareholders in the stock market.

3.2.3.2 Individual shareholders' role in the Thai capital market

The role of minority shareholders in the market is indicated by the number of individual investors and their behaviours.

Table 3.2 Number of shareholders by shareholder types

Types	Dec 2006	Dec 2007	Dec 2008
Thai individuals	902,545	898,958	699,455
Foreign individuals	23,869	24,798	20,997
Thai juristic persons	17,906	17,918	14,135
Foreign juristic persons	5,051	5,463	4,154

Source: Thailand Securities Depository Company Limited

As Table 3.2 shows, approximately only 1.4 per cent of the total Thai population invests in the stock market.⁹⁰ The overall number of individual investors is, in fact, gradually declining. The Thai SEC conducted a survey on small investors regarding an understanding of capital market investment and found that 51 per cent of the

⁸⁹ At the beginning, the Thai secondary market for bonds was organised in 1994 when the Association of Securities Companies (ASCO) set up a Bond Dealers Club (BDC). In 1998 the Club had been reorganised as a separate legal entity, known as the Thai Bond Dealing Centre (ThaiBCD) with permission from the Thai SEC as a licensed bond market. In 2004, due to a large number of bonds issued by the Thai government and financial institutions, the government initiated reform of the Thai bond market. The ThaiBCD therefore had sold its newly developed electronic trading platform to the SET and changed its status and granted the licence of a securities-related association under the Securities Act named as the Thai Bond Market Association (ThaiBMA) in September 2005. *ThaiBMA: About Us* (2009) The Thai Bond Market Association <<http://www.thaibma.or.th/aboutus/aboutus.html>> at 20 March 2012.

⁹⁰ Based on the records of 2010, Thailand's population is about 64 million. National Statistical Office, *Key Statistics of Thailand* (2012) Table 1.3.

respondents were reluctant to invest in securities because of possible loss.⁹¹ A quarter of respondents admitted that they did not know what securities were.⁹² The same study revealed that almost 50 per cent of respondents generally understood the products they invested in while 32.5 per cent of respondents had a very limited knowledge of them.⁹³ The findings explain why Thai individuals prefer depositing their savings in financial institutions rather than in holding securities. Besides, as the Thai government bailed out many financial institutions during the 1997 financial crisis, the impression has been created that the government implicitly guaranteed such deposits.⁹⁴

In addition to the limited understanding of Thai retail investors, the schemes that encourage the distribution of shares to the public are rare. The first government fund, known as Vayupak fund, was set up in 2003.⁹⁵ The fundraising was used to purchase the government's assets. The government then used this money to repay some of its debts. Repayment of investment in the fund is due in 2013 but the government still has no clear policy on extending it or setting up another.⁹⁶ Some state-owned organisations in some industries, such as energy, telecommunications, and transportation, have been privatised. However, the previous privatisations have not been proved successful. The criticisms of privatisations include a lack of consideration of the consequences to the

⁹¹ Corporate Strategy Department SEC, 'Behaviour, Need, Understanding, and Attitude of Thai Investors' (SEC, May 2002). In 2010, a similar survey was conducted. The result affirmed that the main reason that most participants did not invest in financial products was the scare of possible loss. TNS Research International, 'Opportunities in Educating Retail Investors' (Securities and Exchange Commission, 2010) <http://www.sec.or.th/infocenter/report/Content_0000000273.jsp?categoryID=CAT0000291&lang=th> at 20 March 2012.

⁹² Corporate Strategy Department SEC, above n 91.

⁹³ Ibid. The recent study found that 54 per cent of the investors claimed that they were somewhat familiar with all the products they invested in and 20 per cent of them were slightly familiar with the invested products. TNS Research International, above n 91.

⁹⁴ In August 2008 the Deposit Insurance Act came into effect. The Act established a Deposit Insurance Agency to guarantee depositors' funds in the event of a bank bankruptcy. The Agency will pay each depositor all monies shown in every account with a maximum payment of 1 million baht. During the first four years of operation of the Act, the payments to depositors will be secured as follows:

The first year:	the full amount as shown in the account.
The second year:	a maximum payment of 100 million baht.
The third year:	a maximum payment of 50 million baht.
The fourth year:	a maximum payment of 10 million baht.
From the fifth year:	a maximum payment of 1 million baht.

⁹⁵ Veerapong Ramangkul, 'Vayupak Fund: The Financial Innovation', *Bangkok Business* (Bangkok), 14 July 2003, 2 <<http://www.nidambe11.net/ekonomiz/2003q3/article2003july14p3.htm>> at 20 March 2012; 'The Core of Vayupak Fund', *Bangkok Business* (Bangkok), 12 November 2003.

⁹⁶ 'State Enterprise Policy Office Proposes Three Approaches Dealing with Vayupak Fund', *Thairath* (Bangkok), 8 June 2011.

public and a lack of transparency.⁹⁷ Given the resistance of the public, privatisation of state-owned enterprises in other areas, such as electricity and water supplies, has been frozen.

There are changes in the proportion of shares held by institutional and individual shareholders. The first factor is the increasing size of statutory funds. Together with their employers, employees in both public and private sectors are required to distribute some of their wages into statutory funds. The purpose of these funds is to help employees to save some of their salary to be used for different events, such as sickness, unemployment, or retirement. By law, the savings may be used as investments in specified stocks and debentures. The increasing size of statutory funds makes these funds the major equity holders. Secondly, since 2008 the government has encouraged retail investors to invest in long-term mutual funds by granting some tax benefits. It may attract current and new individual shareholders to invest more in mutual funds. These two factors may finally create a tradition of retail investing in Thailand.

The proportion of shares held by various types of shareholders also revealed the limited influence of retail investors in the Thai stock market.

Table 3.3 Holding of equity (2002)

Types of shareholders	Per cent of equity
Social securities funds	0.01
Pension funds	0.08
Provident funds	0.24
Foreign funds	0.55
Insurance companies	1.06
Mutual funds	1.3
Commercial banks	5.16
Other organisations, such as foundations and cooperatives	11
Other financial institutions, such as securities companies	18
Retail investors	21
Corporations	42

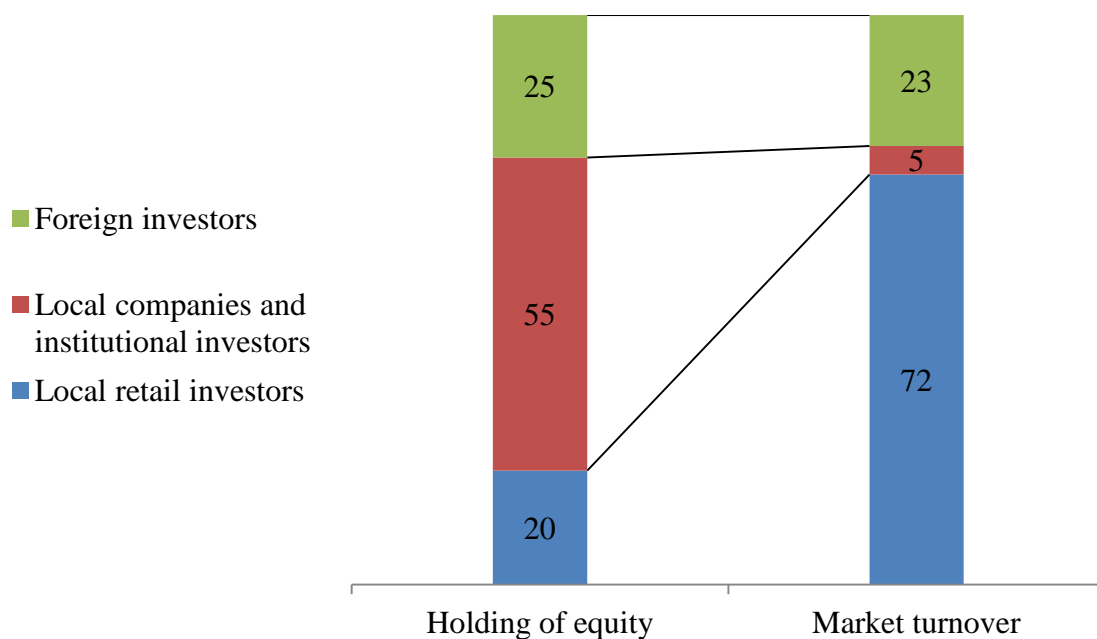
Source: Prasarn Trairatvorakul, *The Necessity and Policy Guidelines to Develop the Thai Capital Market* (2002–2003)

⁹⁷ See Nuntawat Boramanun, 'The Report on Privatisation' (Council of State of Thailand, 2004).

As the above table shows, Trairatvorakul found that the largest strategic investors in the Thai stock market were corporations. The shareholding of this group accounted for 42 per cent of the total market. Retail investors occupied approximately 20 per cent of the market. Trairatvorakul explained that institutional investors were unlikely to invest in the stock market because shares investment was considered high-risk. These institutional investors therefore preferred to invest in low-risk securities, such as debentures.

Trairatvorakul further researched the total turnover of local retail, local institutional and foreign investors compared with their holding of equity.

Figure 3.1 Holding of equity and market turnover compared (2002)



Source: Prasarn Trairatvorakul, *The Necessity and Policy Guidelines to Develop the Thai Capital Market* (2002–2003)

He found that although retail investors held approximately 20 per cent of all equity securities, they traded actively. The total value of securities traded by this group was 75 per cent of the whole market.⁹⁸ By comparison, domestic institutional investors held around 55 per cent of the total value of the market but the value of securities they traded

⁹⁸ Trairatvorakul, above n 77, 103–4.

was only 5 per cent of the total market value.⁹⁹ This reflects the investment behaviour of Thai retail investors. They invest in the market as short-term speculators rather than long-term investors.¹⁰⁰

In all, the research, while dated, shows that the development of the Thai stock market has been mainly influenced by the government. The government established and developed it. Despite the possible changes, the role of individual investors in the Thai capital market has not been evident. They have limited understanding of the equity market and prefer depositing their savings with a bank. The behaviour of current investors also does not support the growth of the market.

3.3 Reforms to minority shareholders' protection in Thailand

The previous section discussed the development of the Thai stock market and the role of retail investors. The following section focuses on reforms to minority shareholders' protection in Thailand. It illustrates which factors have driven reforms and their process and outcomes.

3.3.1 The demand for legal reform in Thailand

According to Berkowitz *et al*, the demand for law is important to the success of legal transplants.¹⁰¹ The demand is necessary as it initiates and implements reform. A strong public demand reflects how the adopted law will be used. It also pushes the responsible institutions to enforce the imported law.

⁹⁹ Ibid.

¹⁰⁰ Fagan pointed out that '[i]n a market with little discipline and no viable legal enforcement to act as a safety net (ie the SET as it stands today), short-term speculation is the best way for retail investors to reduce the risk of losing their investment'. John Fagan, 'The Role of Securities Regulation in the Development of the Thai Stock Market' (2003) 16 *Columbia Journal of Asian Law* 303, 344.

¹⁰¹ Daniel Berkowitz, Katharina Pistor and Jean-Francois Richard, 'The Transplant Effect' (2003) 51 *American Journal of Comparative Law* 163, 189.

3.3.1.1 Government-led policies

As mentioned the severe consequences of the 1997 crisis led to the Thai government requesting financial assistance from international organisations. In exchange for a rescue package offered by the IMF, Thailand was required to make reforms, including to minority shareholders' protection.¹⁰² Thailand was urged to adopt a set of international standards and codes developed by the IMF, the World Bank and the US Treasury Department. Such a set of standards to support free markets, more broadly known as the Washington Consensus, focused on the belief that the free market could effectively allocate resources and discipline corporate management.¹⁰³ In respect of securities regulations, a deregulated market based on disclosure was the preferred option.¹⁰⁴ To heighten the standards of accounting and disclosure, better oversight by independent directors, auditors, and in some cases, by regulators, was required.¹⁰⁵ To assist Thailand in implementing these international standards, the IMF and World Bank suggested Thailand apply the *Principles of Corporate Governance*¹⁰⁶ developed by the OECD as guidelines to further improve its regulatory practices. To ensure compliance

¹⁰² Mak Yun Teen and Cheng Chee Kiong, 'Corporate Governance Practices and Disclosures in Singapore: An Update' (Paper presented at the Second Asian Roundtable on Corporate Governance: The Role of Disclosure in Strengthening Corporate Governance and Accountability, Hong Kong, China, 31 May 2000) <www.oecd.org/dataoecd/6/17/1931014.pdf> at 20 March 2012, 39–40.

¹⁰³ John Williamson, 'Did the Washington Consensus Fail?' (Outline of speech at the Center for Strategic & International Studies, 2002) <<http://www.iie.com/publications/papers/paper.cfm?ResearchID=488>> at 20 March 2012; Moises Naim, 'Fads and Fashion in Economic Reforms: Washington Consensus or Washington Confusion?' (Paper presented at the Conference on Second Generation Reforms, Washington DC, 8–9 November 1999).

Under this concept, the keys for economic success in developing countries are macro-stability, liberalisation, and privatisation. This concept has been heavily criticised. See, eg, 'Unrevealing the Washington Consensus: An Interview with Joseph Stiglitz' (2000) 21 *Multinational Monitor* 4; Dani Rodrik, 'Goodbye Washington Consensus, Hello Washington Confusion? A Review of the World Bank's Economic Growth in the 1990s: Learning from a Decade of Reform' (2006) 44(4) *Journal of Economic Literature* 973. The concept of the market for corporate control is to reduce the managerial slack. There is the relation between corporate managerial efficiency and the market price of shares. The poor performance of the company is a direct outcome of poor management. Poor performing companies will be taken over and slack management will be replaced. See Henry G Manne, 'Mergers and the Market for Corporate Control' (1965) 73(2) *The Journal of Political Economy* 110; Andrei Shleifer and Robert W Vishny, 'Value Maximization and the Acquisition Process' (1988) 2(1) *The Journal of Economic Perspectives* 7.

¹⁰⁴ Fagan, above n 100, 312.

¹⁰⁵ Ibid.

¹⁰⁶ The Principles were firstly released in May 1999 and revised in 2004. The OECD Principles are one of the 12 Key Standards for Sound Financial Systems of the Financial Stability Board. See *12 Key Standards for Sound Financial Systems* (2009) The Financial Stability Board <http://www.financialstabilityboard.org/cos/key_standards.htm> at 20 March 2012.

with international standards the World Bank launched a project to evaluate corporate governance in Thailand using the OECD practices as a benchmark.¹⁰⁷

Another incentive for the Thai government to implement corporate governance reform is to regain the confidence of domestic and international investors and to rebuild its economy. According to the influential works of La Porta *et al*, jurisdictions with poor legal rules and legal enforcement tend to have smaller capital markets.¹⁰⁸ They argued that common law countries have the strongest legal protection for investors while French-influenced civil law countries have the weakest.¹⁰⁹ They further affirmed that there is a correlation between the market value of the firm and the degree of legal protection of minority shareholders.¹¹⁰ Their work suggested that capital markets are most developed in common law countries where the law provides the best protection for minority shareholders against expropriation by controlling shareholders. They indicated that to develop a capital market, emerging countries should consider adopting common law legal models.¹¹¹

La Porta *et al*'s conclusions are reflected in a number of reports of different international firms and organisations. For instance, a McKinsey survey on mutual funds, private equity investors and money managers found that these investors were prepared

¹⁰⁷ World Bank, *ROSC: Reports on the Observance of Standards & Codes* (2009) World Bank, <http://www.worldbank.org/ifa/rosc_more.html> at 20 March 2012.

¹⁰⁸ Rafael La Porta et al, 'Law and Finance' (1998) 106(6) *Journal of Political Economy* 1113, 1151–2.

¹⁰⁹ Ibid; Rafael La Porta et al, 'Legal Determinants of External Finance' (1997) 52(3) *The Journal of Finance* 1131, 1149.

¹¹⁰ Rafael La Porta et al, 'Investor Protection and Corporate Valuation' (2002) 57 *The Journal of Finance* 1147.

¹¹¹ See *ibid*; La Porta et al, *above n 109*; Rafael La Porta, Florencio Lopez-de-Silanes and Andrei Shleifer, 'Corporate Ownership Around the World' (1999) 54(2) *The Journal of Finance* 471; Rafael La Porta et al, 'Agency Problems and Dividend Policies Around the World' (2000) 55(1) *The Journal of Finance* 1; Rafael La Porta et al, 'What Works in Securities Laws?' (2006) 61(1) *The Journal of Finance* 1. Although the works of La Porta *et al* are amongst the most cited in the past decade, the research has been widely criticised. See John C Coffee Jr, 'The Future as History: The Prospects for Global Convergence in Corporate Governance and its Implications' (1999) 93 *Northwestern University Law Review* 641; Troy A Paredes, 'A System Approach to Corporate Governance Reform: Why Importing US Corporate Law isn't the Answer' (2004) 45 *William & Mary Law Review* 1055; Mathias M Siems, 'What Does Not Work in Comparing Securities Laws: A Critique on La Porta et al's Methodology' (2005) *International Company and Commercial Law Review* 300; Mathias M Siems, 'Numerical Comparative Law: Do We Need Statistical Evidence in Law in Order to Reduce Complexity?' (2005) 13 *Cardozo Journal of International and Comparative Law* 521.

to pay premiums for companies with high governance standards.¹¹² The premium for good governance in Thai companies was approximately 26 per cent.¹¹³ The Asian Corporate Governance Association, supported by US investment and pension funds, has also attempted to accelerate the development of corporate governance by evaluating companies and their regulations in the Southeast Asian region. Their conclusions suggested that amendments to laws and regulatory practices were required to advance minority shareholders' protection. Assessing the disclosure practices in the largest listed companies in Thailand, Standard & Poor's and the National University of Singapore found a general lack of disclosure in most companies.¹¹⁴ The effect of the perceived poor protection for minority shareholders became clear in 2002 when CalPERS pulled its investment out of Thailand.¹¹⁵ A report conducted for CalPERS by Wilshire Associates, its financial consultants, rated Thailand low in the categories of transparency, legal systems and investor protection, market liquidity, volatility and transaction costs.¹¹⁶ Thai authorities¹¹⁷ responded that Thailand had made significant progress in corporate governance, accounting standards, the general conduct of businesses and in the enforcement of rules and regulations.¹¹⁸ However, CalPERS did not overturn its decision. Consequently, the Thai stock market dropped 6.7 per cent on the first two days after the announcement of CalPERS' decision.¹¹⁹ This incident accelerates the Thai government to drive regulatory reform.

¹¹² The survey participants included mutual funds, private equity investors, and money managers with an estimated \$US 9 trillion assets under management. Around 90 per cent of their investments were in emerging countries. McKinsey & Company, *Global Investor Opinion Survey: Key Findings* (2002) McKinsey & Company <<http://www1.mckinsey.com/client-service/organization-leadership/service/corp-governance/PDF/GlobalInvestorOpinionSurvey2002.pdf>> at 20 March 2012; McKinsey & Company, *Giving New Lift to the Corporate Governance Reform Agenda for Emerging Markets* (McKinsey & Company <<http://www1.mckinsey.com/client-service/organization-leadership/service/corp-governance/pdf/EmergingMarketOpinion.pdf>> at 20 March 2012; McKinsey & Company, *Investor Perspectives on Corporate Governance – A Rapidly Evolving Story* (2004) McKinsey & Company <www1.mckinsey.com/client-service/organization-leadership/service/corp-governance/pdf/Investor_Perspectives_Corp_Governance.pdf> at 20 March 2012.

¹¹³ McKinsey & Company, above n 112 [Global Investor Opinion Survey]. The figure was from the survey in 2000. The premium for the shares of high-standard Thai companies decreases to 20 per cent.

¹¹⁴ Standard & Poor's and Corporate Governance and Financial Reporting Centre, 'Corporate Governance Disclosures in Thailand: A Study of SET50 Companies' (2004).

¹¹⁵ Thanong Khanthong and Siriporn Chanjindamanee, 'Ethical Divestment: Pensions Giant Exits Thailand', *The Nation* (Bangkok), 2002, 1; Lesley Curwen and Manuela Saragosa, 'US Pension Fund Quits Asian Countries', *BBC* 21 February 2002, 1.

¹¹⁶ Fagan, above n 100, 319.

¹¹⁷ Mainly the Thai SEC.

¹¹⁸ SEC News Release No 7/2002.

¹¹⁹ Bruce Einhorn, 'Will CalPERS Kill Asia's Rally? The Giant California State Pension Fund's Retreat from Southeast Asia Could Lead Other Big Investors to Follow Suit', *Online Asia* 25 February 2002, 1.

3.3.1.2 Demand from the private sector

The above findings indicate the external pressure put on the Thai government to initiate reform. The important issue, according to Berkowitz *et al*, is whether the Thai private sector has pushed for reform. As mentioned in Chapter 2, similar to other Asian companies, Thai companies are dominated by a limited number of wealthy families. This trend had changed after the 1997 financial crisis when a large number of family businesses were affected and some of the controlling shareholders could no longer maintain their large stakes. Suehiro and Natenapha reported that the financial crisis reduced the role of families in controlling listed companies.¹²⁰

Table 3.4 Changes in controlling shareholders of Thai listed companies after the 1997 financial crisis

Ownership types in 1996	Ownership types in 2000	Financial institutions	Non-financial institutions	Total	%
Families	Families	8	160	168	39.6
State	State	2	9	11	2.6
Owned by companies	Owned by companies	15	25	40	9.4
Diffused ownership	Diffused ownership	15	35	50	11.8
Foreign	Foreign	6	39	45	10.6
Unchanged		46	268	314	74.1
Families	Owned by companies	0	5	5	1.2
Families	Diffused ownership	1	16	17	4.0
Families	Foreign	2	16	18	4.2
State	Diffused ownership	1	0	1	0.2
Owned by companies	Families	3	0	3	0.7
Owned by companies	Owned by companies	1	0	1	0.2
Owned by companies	Diffused ownership	3	4	7	1.7
Owned by companies	Foreign	2	3	5	1.2

¹²⁰ Akira Suehiro and Natenapha Wailerdasak, 'Family Business in Thailand: Its Management, Governance and Future Challenges' (2004) 21(1) *ASEAN Economic Bulletin* 81. See also Deunden Nikomborirak and Somkiat Tangkitvanich, 'Corporate Governance: The Challenge Facing the Thai Economy' (Paper presented at the Corporate Governance in Asia: A Comparative Perspective, Seoul, Korea, 3–5 March 1999) Table 2.

Owned by companies	Others	4	0	4	0.9
Diffused ownership	Families	1	7	8	1.9
Diffused ownership	Owned by companies	6	7	13	3.1
Diffused ownership	State	3	0	3	0.7
Diffused ownership	Foreign	9	9	18	4.2
Foreign	Owned by companies	1	6	7	1.6
Changed		37	73	110	25.9
Total		83	341	424	100
Family owned	Others	3	37	40	9.4
Non-family owned	Foreign	13	28	41	9.7

Source: Natenapha Wailerdsak, *Business Groups and Family Business in Thailand before and after the 1997 Crisis* (2006)

To maintain their core businesses, the founders of these companies had to decrease the size of their investment in these companies or hive off parts of the company's business. The above table reveals that, of 208 family-owned companies, 40 families lost their controlling power to the public, other partners, or foreign investors.¹²¹ Even so, Natenapha found that organised control by these families remained strong.

Table 3.5 Controlling shareholders of large Thai listed companies in 1996 and 2000

Types of companies		1996	%	2000	%
Family-owned		150	33.5	131	30.3
Partly family-owned		66	14.7	52	12.0
Diffused ownership		160	35.7	145	33.5
Foreign		59	13.2	90	20.8
State-owned		13	2.9	15	3.5
Total	Listed companies	448	100	433	100
	Family and partly family owned companies	216	48.2	183	42.3

Source: Natenapha Wailerdsak, *Business Groups and Family Business in Thailand before and after the 1997 Crisis* (2006)

As the above table shows, after the 1997 financial crisis the reduction of shareholdings, totally and partly held by family companies is only 5.9 per cent. Consistent with Table 3.4, which shows that the shareholding structure in 39.6 per cent of family-owned companies was unchanged, the increased shareholding by the second largest

¹²¹ See also Natenapha Wailerdsak, *Business Groups and Family Business in Thailand before and after the 1997 Crisis* (2006) 92–3.

shareholders, foreign investors, or the public, is not sufficient to overcome the power of controlling shareholders.

It could be expected that these new shareholders, especially when they were foreign and became the second largest shareholders would have brought changes to governance practices in family-owned companies. They may also have requested legal reforms to corporate and securities law to better protect their interests. The research, however, finds that the role of the second largest or foreign shareholders is limited. This is mainly because the control of majority shareholders remains strong. A legal practitioner explained that:

In my view, the role of the second largest shareholders or foreign investors is varied. This depends on their business policies. Some institutional investors may take part in management while others do not install any new management. The existence of foreign investors possibly influences the company to improve its corporate governance. In addition, to attract investment, some companies try to improve corporate governance at the firm level. Surprisingly some companies do not see corporate governance improvement as necessary. The other factor which is needed to be addressed is the connection between the controlling shareholders and their possible business partners. It is unlikely that controlling shareholders will choose partners who they cannot get along with.¹²²

A professional director also agreed on the continuing strong control of majority shareholders:

I personally see the role of [the second largest shareholders and foreign investors is] not strong. Although controlling shareholders transfer some of their shares to the second largest shareholder or invite foreign shareholders to be their partners, their stake in the company remains very strong. The only exception would be in banking businesses. Because of the financial crisis, banks need an enormous capital to maintain their businesses. Only one or two families are able to maintain their large stake in banks.¹²³

In respect of retail investors it could be expected that minority shareholders who were affected by the financial crisis likewise would have demanded legal reforms. It was

¹²² Interview with a Thai SEC officer, Bangkok.

¹²³ Interview with an independent professional director, Bangkok.

claimed that controlling shareholders and their managerial associates abused their authority to the detriment of minority shareholders. For instance, the former directors of Thai Modern Plastic Industry, one of the largest Thai plastic manufacturers, had borrowed money on behalf of the company, but 2.5 billion baht of the borrowed money was not recorded in the company's accounts.¹²⁴ A former controlling shareholder of MBK shopping mall let some spaces in the mall to his subsidiary companies at a discount price and then these subsidiaries sub-let those spaces the market prices.¹²⁵

Despite these claims, no allegations of mismanagement were ever brought to court. Also, small investors have not expressed their demands to the government for more effective laws. This may be, firstly, because of their small stakes in the company. As Table 3.5 illustrates, the number of companies with diffused shareholdings was reduced. Although the change is very slight, the fact is surprising. Even after the financial crisis, in which controlling shareholders had to distribute their shares to maintain their business, retail investors did not obtain those shares. This may be because the economic bust downturn meant that local retail investors were not in a position to acquire shares. A second explanation for the absence of a demand for reform may be the attitude of the retail investors themselves. A study by Hutthakarhun shows that Thai retail investors averagely hold securities for 36 days. A large number of them trade every week. Some of them trade every day.¹²⁶ Similarly, Songkrietsak found that approximately 62.93 per cent of retail investors invest in the market for less than three months and 16.20 per cent of retail investors buy and sell in the same day.¹²⁷ From these studies, it may be concluded that Thai retail investors consider shares as a potential source for a quick return on a short-term investment.¹²⁸ Given their behaviour, they have limited incentives to seek to initiate legal reforms.

¹²⁴ Securities and Exchange Commission, *SEC: One Decade* (1992) 150; '108 Frauds for Business Persons to Protect their Wealth in the Economic Crisis', *Bangkok Business* (Bangkok), 20 September 1998, 1.

¹²⁵ Patcharapa Changkaew, 'Mahboonkrong through the Storm', *Manager* (Bangkok), June 1991, 1.

¹²⁶ Nitis Hutthakarhun, *Securities Investment Behaviors of Individual Investors in the Bangkok Metropolitan Area* (MBA Thesis, Srinakharinwirot University, 2005) 113–4. The issue of high frequency trading is recently addressed. See Eugene Clark, 'The Legal Tortoise and the High Frequency Trading Hare: The Challenge for Regulators' (2011) 25 *Australian Journal of Corporate Law* 274.

¹²⁷ Piboon Songkrietsak, *Securities Investment Behaviors of Individual Investors* (M Econ Thesis, Thammasat University, 2000) 66. Cf Maesatri Boontang, *Behaviour of Retail Investor in Stock Exchange of Thailand in Bangkok Metropolitan* (M Management Thesis, Suan Dusit Rajabhat University, 2005).

¹²⁸ Ibid.

In summary, the demand for better legal protection for minority shareholders is mainly found in the public sector. Influenced by international organisations, regulatory reform has been seen as necessary to obtain finance to assist the state during crisis and to also attract investment and to regain the confidence of investors at both local and international levels. In the private sector, the evidence shows that even after the 1997 financial crisis, the control over companies by majority shareholders remains strong. Some shares are distributed to the second largest shareholders and foreign investors. However, they cannot overcome the power of the existing controlling shareholders. The role of retail investors in driving reform has not been evidenced. They have no incentive to pressure the government for better protection, as they are generally short-term speculators rather than long-term investors. Without a strong demand from minority shareholders, it is questionable whether legal reform will be successful. The following section discusses the process of the reform and illustrates what has been done to improve corporate governance practice in Thailand.

3.3.2 Post-1997 crisis reform

The consequence of the 1997 financial crisis and the strong demand made on the Thai government led to the reform of minority shareholders' protection. Watson defined this situation as a voluntary transplant.¹²⁹ Miller explains that a transplant may take place through the motivation of a recipient jurisdiction to satisfy foreign states, individuals, or entities.¹³⁰ This includes the situation where a country accepts a condition of adopting a model law designed by the creditor country or organisation in exchange for financial support.¹³¹ The reform of corporate governance and minority shareholders' protection in Thailand has mainly taken in three forms: the establishment of organisations to improve corporate governance; the adoption of a code of corporate governance; and the changes to legislations as dealt with in Section 3.4 below.

¹²⁹ Alan Watson, *Legal Transplants: An Approach to Comparative Law* (1974) 29.

¹³⁰ Jonathan M Miller, 'A Typology of Legal Transplants: Using Sociology, Legal History and Argentine Examples to Explain the Transplant Process' (2003) 51 *American Journal of Comparative Law* 839, 847–9.

¹³¹ Ibid.

3.3.2.1 Institutions

Before 1997 the organisations which played a significant role in monitoring the Thai stock market were the SET itself and the Thai SEC. Due to the severe impact of the 1997 crisis on the Thai capital market, the Thai government took action to prevent a reoccurrence. It initiated consultations to obtain knowledge and opinions from the public as well as private organisations.¹³² Finally, in 2002 the cabinet established the National Corporate Governance Committee to establish policies and processes to upgrade the level of regulation and corporate governance.¹³³ The members of this Committee came from both public agencies and the private sector.¹³⁴ The government also announced that 2002 as the year of corporate governance. The Thai SEC, as the state regulator, established the Director Responsibilities Steering Group in 2004 to assist the Thai SEC to reduce the potential for future wrongdoings.¹³⁵ If a director's action breaches the law, the Thai SEC forwards the case to a public prosecutor. If such actions are not illegal but considered inappropriate, the Steering Group calls such a director for clarification. If the director persists with inappropriate conduct, the Steering Group may propose to the Thai SEC that the director be removed from the database of permitted directors and executives of securities issuing companies.¹³⁶ The consequence of being removed from the database is severe. According to the listing rules, a company with such a director itself is no longer able to offer securities or to be listed.¹³⁷ The SET established the Corporate Governance Center to assist listed companies in improving their corporate governance systems.¹³⁸ The Center publishes guidelines and holds

¹³² *CG Information*, Securities and Exchange Commission <http://www.sec.or.th/CG/Content_0000000086.jsp?categoryID=CAT0000241&lang=en> at 20 March 2012.

¹³³ *Appointment of National Corporate Governance Committee* (2009) National Corporate Governance Committee <http://www.cgthailand.org/SetCG/about/ncgc_en.html> at 20 March 2012.

¹³⁴ Including the representatives from the cabinet, Bank of Thailand, the Thai SEC, the SET, Listed Companies Association, Thai Investors' Association, and Thai Institute of Directors' Association.

¹³⁵ SEC News Release No 17/2004, 29/2004.

¹³⁶ In 2004 the SEC reported the successful outcome of the Steering Group in terminating inappropriate actions found in five listed companies, such as conflict of interest and connected lending. These transactions were worth approximately three billion baht. SEC News Release No 35/2004. The database of directors and executives of securities issuing companies was created in 2005. All of the directors in listed companies must register their names into the system. The database can be publicly accessed.

¹³⁷ *Ibid.*

¹³⁸ *Corporate Governance Center* (2009) The Stock Exchange of Thailand <http://www.cgthailand.org/SetCG/about/ncgc_en.html> at 20 March 2012.

activities to educate directors and executives.¹³⁹ In addition, the Thai Institute of Directors Association was founded and financially supported by the Thai SEC, the SET, the Bank of Thailand, the Foundation for Capital Development Fund, and the World Bank to improve the professionalism of directors and corporate governance more generally.¹⁴⁰

To further regain local and foreign investors' confidence, in 2002 the Minister of Finance, together with the Thai SEC and the SET, created the Thai Investors Association.¹⁴¹ The core functions of the Association are to protect and educate small shareholders. It has acquired a small holding of equity shares in all listed companies so that it can participate in the shareholders' meetings.¹⁴² Every year the Association conducts a survey, the Annual General Meeting Assessment Project, to evaluate whether minority shareholders can adequately exercise their rights in these meetings.¹⁴³ In addition, the Thai SEC appointed Thailand Ratings and Information Systems (TRIS) Corporation to rate corporate governance systems within listed companies.¹⁴⁴ The Thai SEC encouraged listed companies to participate in this project by reducing various fees collected by the Thai SEC and the SET to corporations with good ratings.¹⁴⁵ Unfortunately, only seven companies participated¹⁴⁶ and the program was terminated in 2005 because of this.¹⁴⁷

¹³⁹ Ibid.

¹⁴⁰ *About IOD* (2009) Thai Institute of Directors <<http://www.thai-iod.com/en/aboutIOD.asp>> at 20 March 2012.

¹⁴¹ Back in 1983, 50 experienced investors set up the Thai Investor Club as an information centre for shareholders in listed companies. Later, in 1989 the Investor Club had its organisation registered and changed its name to Thai Investor Association. See *History of the Association* (2009) Thai Investor Association <<http://www.thaiinvestors.com/index.php?lay=show&ac=article&Id=538662239>> at 20 March 2012.

¹⁴² Deunden Nikomborirak, 'Building Good Corporate Governance After the Crisis: The Experience of Thailand' in Ho Khai Leong (ed), *Reforming Corporate Governance in Southeast Asia: Economics, Politics, and Regulations* (2005) 215–6. The author argued that the effectiveness of the Thai Investor Association was still unclear.

¹⁴³ *AGM Assessment Project* (2009) Thai Investor Association <http://www.tris.co.th/index.php?option=com_content&task=view&id=43&Itemid=70> at 20 March 2012.

¹⁴⁴ TRIS was set up by the Minister of Finance and the Bank of Thailand. Later, it was approved by the Thai SEC to rate the credit worthiness of corporations and state-owned enterprises. *History of TRIS Corporation* (2012) TRIS Corporation <<http://www.tris.co.th/detailcompany/story.html>> at 20 March 2012.

¹⁴⁵ Nikomborirak, above n 142, 215.

¹⁴⁶ *Corporate Governance: Rating* (2012) <<http://www.tris.co.th/service/customertris/19-user.html>> at 20 March 2012. These seven companies are large widely-held companies.

¹⁴⁷ Vincent Siew, *Protection of Minority Shareholders in Public Listed Companies in Thailand* (DBA Thesis, University of South Australia, 2008) 46.

3.3.2.2 Code of corporate governance

Prior to the 1997 financial crisis there were no codes or guidelines on corporate governance or best business practices in Thailand. In October 1999 the SET issued the *Code of Best Practice for Directors of Listed Companies*, setting the guidelines for board members as shareholders' representatives.¹⁴⁸ It introduced mechanisms intended to provide better protection for minority shareholders, such as the appointment of outsiders to the board of directors,¹⁴⁹ revised processes for appointing directors, and setting directors' remuneration.¹⁵⁰ In 2002 the SET published the *15 Principles of Good Corporate Governance* for listed companies to implement.¹⁵¹ Kouwenberg observed that the voluntary corporate governance code adopted in Thailand was influenced by the *Code of Best Practice* issued by the Cadbury Committee.¹⁵² The 15 Principles address several issues relating to the protection of minority shareholders, such as the concept of the equitable treatment of shareholders,¹⁵³ the independence of directors,¹⁵⁴ and internal review and control mechanisms.¹⁵⁵ Listed companies have been required to demonstrate how they apply these 15 principles. In the case of non-application, the companies are required to provide justifications where they do not comply with them.

The development of a voluntary code of corporate governance underwent a significant change in 2005 when the Thai government, through the Thai SEC, entered into the Report on the Observance of Standards and Codes (ROSC) project. Thai regulations and codes of corporate governance were evaluated by the World Bank. The Principles of Corporate Governance¹⁵⁶ developed by the OECD were applied in the evaluation.¹⁵⁷

¹⁴⁸ Stock Exchange of Thailand, *Code of Best Practice for Directors of Listed Companies* (1999).

¹⁴⁹ Ibid Guideline 1.

¹⁵⁰ Ibid Guideline 3, 5.

¹⁵¹ Stock Exchange of Thailand, *The 15 Principles of Good Corporate Governance for Listed Companies* (2002).

¹⁵² Roy RP Kouwenberg, *Does Voluntary Corporate Governance Code Adoption Increase Firm Value in Emerging Markets? Evidence from Thailand* (2006) Social Science Research Network <<http://ssrn.com/abstract=958580>> at 20 March 2012, 9.

¹⁵³ Ibid Principle 2.

¹⁵⁴ Ibid Principle 8.

¹⁵⁵ Ibid Principle 13.

¹⁵⁶ See Organisation for Economic Co-operation and Development, *OECD Principles of Corporate Governance* (2004).

¹⁵⁷ World Bank, *Report on the Observance of Standards and Codes (ROSC): Corporate Governance Country Assessment: Thailand* (World Bank, 2005) viii.

The assessment revealed the weaknesses, especially in the area of the equitable treatment of shareholders, the role of stakeholders in corporate governance, and the responsibilities of the board.¹⁵⁸ The project pointed out that in these areas the Thai legal and regulatory framework largely complied with the OECD Principles but practices and enforcement did not.¹⁵⁹ Less than one year after the report had been released, the SET announced the *Principles of Good Corporate Governance* as a revised version of the 15 Principles.¹⁶⁰ This version was influenced by both the international standards developed by the OECD and the results of the ROSC project.¹⁶¹ The Principles attempted to strengthen minority shareholders' rights by introducing mechanisms to protect them and to facilitate the implementation of those principles.¹⁶²

To summarise, reforms of minority shareholders' protection in Thailand has been initiated and driven by the Thai government under the influence of international organisations. The process of the reform is therefore taking place in the public sector, including the establishment of related organisations to accelerate improved corporate governance at the firm level. A voluntary code of corporate governance has also been created. The code has been revised to meet international standards. Interestingly, the demand from the public or affected retail investors has not been evidenced. There is no independent or privately funded organisation that represents retail investors.

3.4 Thai corporate and securities laws on protecting minority shareholders

As the main focus of the research is on the legal framework for minority shareholders' protection, this section aims to provide a brief outline of Thai laws and regulations relating to their protection. The discussion also seeks to give a fundamental understanding of, and background to, related Thai regulatory policies and processes. To avoid repetition this section provides only a broad view of related regulations, while the

¹⁵⁸ Ibid.

¹⁵⁹ Ibid 1.

¹⁶⁰ Stock Exchange of Thailand, *The Principles of Good Corporate Governance for Listed Companies* (2006).

¹⁶¹ Ibid the introduction page.

¹⁶² For instance, the board of directors is obliged to ensure that all relevant information delivered to all shareholders is correct and timely. Ibid Principle 1. In terms of the composition of the board of directors, the principles suggest that one-third of the board should be independent directors. Ibid Principle 5. The details on the definition of independent directors are discussed in Chapter 4.

details of these provisions will be discussed later in the fourth to the seventh chapters. Thai laws to be discussed in this section are corporate law, securities law, regulations of the Thai SEC, and regulations and listing rules of the SET.

3.4.1 Corporate law

The principal Thai company law is Book three of the Civil and Commercial Code. The Code was enacted in 1925, governing private companies.¹⁶³ In 1978 the Public Companies Act was enacted to provide a more appropriate framework for public companies.¹⁶⁴ The main purpose of the enactment is to allow the establishment of public companies to promote economic development. The Public Companies Act of 1978 was entirely revised and replaced by the Public Limited Companies Act of 1992 (“PLC Act”). The PLC Act imposes requirements on establishing companies, issuing shares, shareholders’ rights, directors’ duties, and penalties for contravention. The Act has been amended twice, in 2001 and 2008. In the first amendment, three significant modifications were made: the abolition of minimum share values;¹⁶⁵ the insertion of share buy-back provisions;¹⁶⁶ and, the insertion of provisions allowing a company to use capital in its reserve accounts.¹⁶⁷ The purpose of the amendment is to increase the flexibility of the operation of public companies and to attract investors back to the Thai equity market to help its recovery. The latest amendment was in 2008 with only one new provision inserted. The Act allows the Director-General of the Department of Business Development to prescribe the amount of fine when a person commits an offence for which there is only a monetary penalty,¹⁶⁸ as these are minor offences.

¹⁶³ The discussion on the development of the Thai Civil and Commercial Code is in Chapter 8.

¹⁶⁴ The history of the emergence of Thai company law is discussed in Chapter 3.

¹⁶⁵ Public Limited Company Act B.E. 2535 (1992) (Thailand) s 50.

¹⁶⁶ Ibid s 66/1.

¹⁶⁷ Ibid s 119; the reserve account is created from (i) profit when a company offers shares at a higher price than its registered value; (ii) at least five per cent of the annual net profit. Ibid ss 51, 116.

¹⁶⁸ Ibid s 222/1. Such offences include the promoters’ failure to submit documents relating to public offerings to the Registrar (ibid s 25); the promoters’ failure to call a meeting after the subscribed shares were sold to the public (ibid s 27); the board of directors’ failure to inform the Registrar when the register of shareholders is lost or defaced (ibid s 62).

3.4.2 Securities law

The other significant law providing protection for minority shareholders is the securities law. The first securities law was enacted in 1974, the Securities Exchange of Thailand Act. The Act was largely influenced by a report called *A Capital Market in Thailand*, produced by Robbins, the former chief economist of the US SEC.¹⁶⁹ The main purpose of this Act was to establish the first Thai government-supported stock market. The Act was amended in 1984 in order to provide additional protection for market traders.¹⁷⁰ Later, it was repealed by the Securities and Exchange Act of 1992 (“Securities Act”). This Act was enacted to revise all securities laws and regulations, reorganise institutions relating to securities trading, and provide more effective protection to investors. The Act imposes specific provisions on public companies listed on the stock market, and extend to the issuing of securities, public offerings, securities businesses, futures and options markets, takeovers, and, penalties for violations. It also established the regulatory body, the Thai SEC.

The Securities Act was amended in 1999, 2003, and 2008. The first amendment was to expand the application of the Act to the management of employees’ provident funds.¹⁷¹ The second one was to allow mutual funds to invest in the futures market.¹⁷² The latest amendment inserted a number of provisions and revised others to provide better protection for minority shareholders. This revision was strongly influenced by the capital market regulation assessment project under the Financial Sector Assessment, initiated by the IMF and the World Bank. This project was to ensure Thailand’s compliance with international standards. In terms of securities regulations, Thailand had followed the report on Detailed Assessment on the Implementation of the International Organisation of Securities Commissions Objectives and Principles of Securities Regulation.¹⁷³ The incorporated provisions can be classified into two categories: those

¹⁶⁹ The Stock Exchange of Thailand, above n 76; see also Robbins, above n 79.

¹⁷⁰ Securities Exchange of Thailand Act B.E. 2517 (1974) (revised B.E. 2527) (1984) (Thailand).

¹⁷¹ Securities and Exchange Act B.E. 2535 (1992) (Thailand) Part 8.

¹⁷² Ibid s 4.

¹⁷³ See The report of the Office of the Council of State no 746/2550; *Implementation of the IOSCO Objectives and Principles of Securities Regulation* (2009) Securities and Exchange Commission <http://www.sec.or.th/sec/Content_0000000021.jsp?categoryID=CAT0000427&lang=en> at 20 March 2012.

which expressly give additional rights to minority shareholders, and those which ensure good corporate governance by imposing responsibilities on related participants in listed companies. The several rights of minority shareholders added in this amendment include the right to propose agenda items at shareholders' meetings;¹⁷⁴ the right to lodge claims against directors who fail to perform their duties;¹⁷⁵ and, the right to revoke a resolution of the shareholders' meetings.¹⁷⁶ To strengthen internal control, the Securities Act clarifies the duties of directors¹⁷⁷ and imposes duties on related participants, such as auditors¹⁷⁸ and secretaries¹⁷⁹ to monitor the management. The concept of the duties of auditors and secretaries was inspired by legal provisions in Australia, Singapore, the UK, and the US.¹⁸⁰ In addition, provisions on whistleblower protection were incorporated.¹⁸¹ This was influenced by US law, the Public Interest Disclosure Act of 1998 and the Sarbanes-Oxley Act of 2002.¹⁸²

¹⁷⁴ Under the PLC Act, the shareholders holding not less than one-third of shares may request the shareholders' meeting to consider other additional matters. (The PLC Act s 105) The revised Securities Act allows shareholders holding not less than five per cent of shares may submit a written proposal to the board of directors to include such a proposal as an agenda item of the shareholders' meeting. (The Securities Act s 89/23)

¹⁷⁵ In the case where the company does not take an action against the misconduct of directors, shareholders holding not less than five per cent of shares may give written notice to the company to make such a claim. If the company fails to comply with the request, such shareholders may take legal action to claim compensation on behalf of the company. (The PLC Act s 85) The revised Securities Act imposes that the right to lodge the claims still exists and the shareholders who bring a legal action in good faith also have the right to be reimbursed for the costs of legal action by the company. (The Securities Act s 89/18)

¹⁷⁶ If the meeting is convened or a resolution is passed without compliance with or in violation of the articles of association of the company or the provisions of the PLC Act, not less than five shareholders or shareholders amounting to less than one-fifth of the total number of sold shares may request the court to order revocation of such a resolution of the meeting. (The PLC Act s 108) The revised Securities Act affirms the right to lodge the claims but reduces the threshold of eligible shareholders to shareholders holding not less than five per cent of shares. (The Securities Act s 89/30)

¹⁷⁷ Under the PLC Act, directors are obliged to perform their duties in good faith and with care to maintain the interests of the company. (The PLC Act s 25) However, the term "in good faith and with care" has not been defined. The Securities Act adopts the concept of Business Judgment Rules to provide a clear view on directors' liabilities. (The Securities Act ss 89/9–14)

¹⁷⁸ The Securities Act s 89/25. The duty of auditors is to inform the audit committee of the company when any suspicious circumstances have been found that do not exist in the PLC Act or the pre-2008 version of the Securities Act.

¹⁷⁹ The revised Securities Act requires a listed company to appoint a company secretary to maintain all company documents. (The Securities Act s 89/15)

¹⁸⁰ 'Companies' Secretaries: VIPs of Thai Listed Companies', *Siamrath* (Bangkok), 24 December 2007; 'Auditors: The Gatekeeper', *Manager* (Bangkok), 8 October 2007.

¹⁸¹ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/2.

¹⁸² 'Whistle Blower Protection: The Wind of Truth?', *Siamrath* (Bangkok), 10 December 2007.

3.4.3 Regulations of the Securities and Exchange Commission

Under the Securities Act, the Securities and Exchange Commission is the core authority regulating all capital market activities. The Thai SEC regulations cover not only directors of listed companies but also securities companies, auditors, asset valuers, brokers, and advisors to ensure that the PLC Act and the Securities Act are complied with. The Thai SEC is empowered to enact regulations to ensure fair securities trading. Its regulations extend to other activities, such as the acquisition of securities in mergers and acquisitions,¹⁸³ and the acquisition or disposal of securities of the company.¹⁸⁴

3.4.4 Regulations and listing rules of the Stock Exchange of Thailand

The regulations of the SET focus on trading in the secondary stock market. They mainly govern the listing of companies, trading activities, and the conduct of members of the market. In regard to minority shareholders' protection, the SET imposes both regulations and guidelines for listed companies to ensure active, fair and orderly securities trading and provide investors with prompt access to information. The regulations include the policies and rules on disclosure of information by both periodic and continuous disclosure,¹⁸⁵ best practice guidelines for audit committees,¹⁸⁶ and the code of best practice for directors of listed companies.¹⁸⁷ Listed companies are contractually obligated to comply with the listing rules. To enforce the rules, there is the Enforcement Unit within the SET that examines any violation and issues a punishment order.

¹⁸³ SEC Notification No GorJor. 53/2545.

¹⁸⁴ SEC Notification No KorChor. 58/2545.

¹⁸⁵ For the full list of regulations on disclosure, see <http://www.set.or.th/set/notification.do?idLv1=1&idLv2=11&language=en&country=US>.

¹⁸⁶ Best Practice Guidelines for Audit Committee of the SET Bor.Jor./Ror.25-00.

¹⁸⁷ Policy Statement of the SET Bor.Jor./Ror.26-00.

3.5 Securities regulator and law enforcement agencies

The following sections cover the core organs enforcing company and securities laws and related regulations – the Thai SEC and other legal enforcement agencies.

3.5.1 The Securities and Exchange Commission

The Thai SEC is established by the Securities Act to supervise securities businesses in the Thai capital market.¹⁸⁸ Within the organisation there are three divisions: the Thai SEC, the Capital Market Supervisory Board, and the Office of the Securities and Exchange Commission.

The Thai SEC comprises four members appointed by the Cabinet¹⁸⁹ and at least six of the members appointed by the Selection Committee.¹⁹⁰ The Thai SEC is empowered to make rules and regulations, and to issue orders to maintain confidence in the stock market.¹⁹¹ When there are reasonable grounds to suspect offence, the Thai SEC is authorised to investigate and take both administrative and criminal actions against wrongdoers. The administrative actions include notices for rectification, warnings, probation, and the suspension of an approval for a specified period of time, or the revocation of an approval.¹⁹² In regard to criminal offences, if the offences do not have a significant impact on the public, the Thai SEC can fine the wrongdoers by presenting the case to the Settlement Committee.¹⁹³ For offences with a significant impact¹⁹⁴ or

¹⁸⁸ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 14.

¹⁸⁹ Which are the Chairman of the Thai SEC appointed by the Cabinet upon the recommendation of the Minister of Finance, the Permanent Secretary of the Ministry of Finance, the Permanent Secretary of the Ministry of Commerce, and the Governor of the Bank of Thailand. Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 8.

¹⁹⁰ For the process of the committee section, see Securities and Exchange Act B.E. 2535 (1992) (Thailand) Chapter 1, Division 3. Section 8 of the Securities Act imposes that the number of experts shall be at least four but not exceeding six people appointed through nomination in accordance with Section 31/7 as commissioners, among whom there shall be at least one legal expert, one accounting expert and one financial expert.

¹⁹¹ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 14.

¹⁹² *SEC in Brief: Inspection and Enforcement* (2009) Securities and Exchange Commission <http://www.sec.or.th/sec/Content_0000000324.jsp?categoryID=CAT0000430&lang=en> at 20 March 2012. If the offender disagrees with the decision made by the SEC, he may bring the case to the Administrative Court within 90 days after the order is made. See http://www.sec.or.th/enforcement/admin_chart.pdf.

¹⁹³ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 315/1.

where the offenders refuse to comply with the order of the Settlement Committee, the Thai SEC must file criminal complaints with the Thai police for further investigation and criminal prosecution.¹⁹⁵ The Thai SEC, unlike some other national regulators, has no power to bring any civil proceeding for compensation on behalf of investors.¹⁹⁶ The details and discussion of the powers of the securities regulators in recovering damages on behalf of affected shareholders are covered in Chapter 7.

The second division is the Capital Market Supervisory Board. It was established in 2008 by an amendment to the Securities Act to assist the Thai SEC in making new and improving existing regulations. The members of the Board are appointed by the Minister of Finance through a nomination process.¹⁹⁷ The core power of the Supervisory Board is to make rules on specific matters including securities issuance,¹⁹⁸ disclosure,¹⁹⁹ related-party transactions,²⁰⁰ including procedures for approving related-party transactions by shareholders' meeting,²⁰¹ and mergers and acquisitions.²⁰² The final division is the Office of the Thai SEC.²⁰³ The head of the Office is the Secretary-General who is appointed by the Minister of Finance on the recommendation of the Thai SEC.²⁰⁴ The major duty of the Office is to implement and enforce the regulations imposed by both the Thai SEC and the Capital Market Supervisory Board.²⁰⁵

Prior to the amendment of the Securities Act in 2008 there was some confusion over the jurisdictional boundaries of the Thai SEC and SET. The SET was founded in 1975 and had full control over listed companies from 1975 to 1992, when the Thai SEC was

¹⁹⁴ See *ibid* s 317.

¹⁹⁵ Securities and Exchange Commission, above n 192. If the offender disagrees with the decision made by the SEC, he may bring the case to the Administrative Court within 90 days after the order is made. See *The Procedure on Administrative Appeal* (2010) Securities and Exchange Commission <http://www.sec.or.th/enforcement/admin_chart.pdf> at 20 March 2012.

¹⁹⁶ Securities and Exchange Commission, above n 192.

¹⁹⁷ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 16/1. The members comprise the Secretary-General as Chairperson, a Deputy Secretary-General, a Director-General of the Fiscal Policy Office and, not exceeding four in number, experts.

¹⁹⁸ *Ibid* ss 35, 41.

¹⁹⁹ *Ibid* s 56.

²⁰⁰ *Ibid* s 89/12.

²⁰¹ *Ibid* ss 89/27–9.

²⁰² *Ibid* Chapter 8, Division 2.

²⁰³ *Ibid* s 17.

²⁰⁴ *Ibid* s 20.

²⁰⁵ *Ibid* s 19.

established.²⁰⁶ The Thai SEC also had a number of powers over companies listed or issuing securities after that date. The resulting regulatory overlap caused jurisdictional confusion to listed companies and in the supervision of the stock market. The Thai SEC and SET therefore entered into a Memorandum of Understanding in 2000 to clarify the role of the Thai SEC as the sole market supervisor.²⁰⁷ However, some confusion still remained.²⁰⁸ Eventually, the Securities Act of 2008 gave the Thai SEC full power to supervise all listed companies. In addition, the Thai SEC is allowed to order the SET to issue, revoke or modify the rules of the SET when it is found that the rules may cause harm to the public interest.²⁰⁹

3.5.1.1 Criticisms of the Securities and Exchange Commission

As a rule maker, principal regulator and market supervisor, the Thai SEC plays a significant role in supervising all listed companies, investigating the activities of these companies, and issuing relevant regulations. All decisions made by the Thai SEC should be reasonable, impartial and in accordance with the laws. Its decision-making processes should be transparent. The Thai SEC should also operate independently of government control to avoid political influence.²¹⁰ These are considered necessary to secure investor's confidence in the market.

The Thai SEC conducted a survey in 2005 to evaluate the public's perception of its image and performance in supervising the capital market and improving corporate governance practice in listed companies.²¹¹ The study revealed that sample institutions, such as securities companies, listed companies, financial advisors, accounting companies, and investors were generally satisfied with its performance. Compared with previous years, the performance of the Thai SEC was perceived to have improved.²¹² However, the issue on which the Thai SEC received the lowest score was the

²⁰⁶ Fagan, above n 100, 325.

²⁰⁷ SEC News Release No 22/2543.

²⁰⁸ Fagan, above n 100, 326.

²⁰⁹ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 170/1.

²¹⁰ Fagan, above n 100, 326–7.

²¹¹ Securities and Exchange Commission, *Satisfaction of the Effectiveness and Public Image of the SEC* (2005) Securities and Exchange Commission, <http://www.sec.or.th/infocenter/th/research/corporate_image.pdf> at 20 March 2012.

²¹² Ibid 4.

transparency of the organisation itself.²¹³ The institutions sampled questioned the integrity of both the Thai SEC's decision-making process and its officers.²¹⁴

The main factor affecting the integrity and independence of the Thai SEC is its structure. Under the previous Securities Act in its organised form, the chairman of the Thai SEC was the Minister of Finance and the other members of the Thai SEC were appointed by the Cabinet pursuant to the recommendation of the Minister of Finance.²¹⁵ In addition, any subordinate legislation proposed by the Thai SEC had to be submitted to the Minister of Finance for approval.²¹⁶ It may be argued that this power was appropriate, as the government desired to grow the capital market and may have viewed some regulations as an impediment to its development. However, the perceived intervention by the government in regulating the market may have had a negative effect.²¹⁷ Therefore, it is necessary for the securities regulator to be seen to be independent from government pressure.

To ensure the integrity of the Thai SEC, the revised Securities Act limits government control over the Thai SEC by specifying that the Cabinet appoints the members of the Thai SEC through a nomination process.²¹⁸ The revised Act further states that members of the Thai SEC cannot be elected officials or hold any position in a political party.²¹⁹ The separation between political parties and the market supervisor is intended to be observed in future by the Cabinet. This would allow the Thai SEC to operate independently and this may improve its public reputation for independence.

Perceived political influence has led to several scandals around the independence and effectiveness of the Thai SEC before the most recent reform. The most prominent was the sale of Advance shares. It is related to a takeover deal in 2006 between Shin Corporation, the majority shares of which were held by the family of the former prime

²¹³ Ibid 9.

²¹⁴ Ibid.

²¹⁵ See Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 8.

²¹⁶ Fagan, above n 100, 326.

²¹⁷ Rangsan Thanapornpun, 'Why should the BOT and SEC be independent?', *Manager* (Bangkok), 26 November 2006, 1.

²¹⁸ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 8.

²¹⁹ Ibid s 9(4).

minister, Thaksin, and Temasek Holdings, the Singapore government-owned investment fund. As a result of widespread rumours about a possible takeover, the shares of Advance Info Service (“Advance”), the holding company of Shin Corp, went from 98 baht to 112 baht. Yingluck, Thaksin’s sister, a managing director of Advance and the majority shareholder in Shin Corp, sold around 278,400 shares six weeks before the takeover at approximately 101 to 113 baht per share.²²⁰ After the takeover, Temasek, the new largest shareholder in Shin Corp, made a tender offer to minority shareholders to acquire all shares at only 72.31 baht per share, about 40 per cent lower than the current market price.²²¹ It was suspected that Yingluck had sold her shares as she was aware that Temasek would make an offer at a lower price.²²² The Thai SEC investigated the case and concluded that Yingluck did not use inside information in trading her shares.²²³ The decision of the Thai SEC was widely criticised. It was claimed that Yingluck, in her capacity as the major shareholder of Shin Corp, should have known of the takeover deal and had sold her shares based on that information.²²⁴ The Thai SEC responded by explaining that it was important to prove that: (i) Yingluck should have known about the takeover deal; (ii) she sold shares; and (iii) she had used the information she possessed. It had concluded that there was not sufficient evidence showing that Yingluck had used inside information.²²⁵ Hence, the Thai SEC was unable to bring an action against her in spite of the public perception of wrongdoing.²²⁶ The critics of the Thai SEC argued that a common problem in dealing with insider trading was the difficulty to prove that inside information had been used.²²⁷ Although Yingluck continually sold shares over the last two years before the month in which the takeover deal took place, it was inexplicable why she suddenly decided to sell 74 per cent more

²²⁰ “Tracking Yingluck unloaded ADVANCE shares – insider trading?”, *Prachachat* (Bangkok), 30 January 2006, 1.

²²¹ Ma Nok and Dek Nok Krob, ‘Yingluck Ruling Shows Watchdog Failing the Public’, *Bangkok Business* (Bangkok), 1 May 2006, 1 <<http://www.thailandqa.com/forum/showthread.php?t=13809>> at 20 March 2012.

²²² Ibid; ‘Freed-up SEC will Mean Fairness for All’, *The Nation* (Bangkok), 13 November 2006, 1 <<http://www.nationmultimedia.com/home/Freed-up-SEC-will-mean-fairness-for-all-30018777.html>> at 20 March 2012.

²²³ SEC News Release No 31/2550.

²²⁴ Ma Nok and Dek Nok Krob, above n 221.

²²⁵ See Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 241.

²²⁶ Thirachai Phuvanatanarubala, *Regarding the Article on Insider Trading of ADVANC Shares* (2006) Securities and Exchange Commission <http://www.sec.or.th/infocenter/th/pub/headlines/letterto_nation.doc> at 20 March 2012.

²²⁷ Ma Nok and Dek Nok Krob, ‘Open Letter to the SEC: After the SEC Judgement was Affirmed’, *Bangkok Business* (Bangkok), 3 May 2006, 1.

shares than she had sold in the previous year. The Thai SEC responded by reiterating that under Thai law it was necessary to prove that the insider used inside information and in this case it was unclear.²²⁸ Later, the Thai SEC suggested that the regulation should be amended to cover situations like this.²²⁹

3.5.2 Thai legal enforcement agencies

In terms of civil actions, similar with German law and practice, the Thai SEC itself is not entitled to bring any civil litigation under the Securities Act.²³⁰ The detailed discussion in this issue is in Chapter 7. Only a shareholder or shareholders²³¹ with five per cent of voting shares of a company who suffer from a securities violation may bring a derivative action on behalf of the company against a director involved in misconduct.²³² The expenses incurred may be reimbursed by the company if the court finds that a lawsuit is brought in good faith. Regarding the use of legal enforcement by minority shareholders, a corporate lawyer explained:

Small investors normally do not file lawsuits. This is because firstly they do not see that the lawsuit financially benefits for them. Secondly, a lawsuit is expensive and consumes a lot of time. Given their small stakes in companies, many minority shareholders prefer to sell their shares rather than to seek legal relief.²³³

In respect of criminal prosecutions, the Thai SEC also has no power to prosecute on its own behalf.²³⁴ As mentioned, in cases of offences with a significant impact on the public, or by those not within the jurisdiction of the Settlement Committee, or who refuse to appear before the Settlement Committee, the Thai SEC has to pass the case to other authorities for further investigation. For offences relating to corporate fraud,

²²⁸ Thirachai Phuvanatanarubala, *Regarding the Open Letter* (2006) Securities and Exchange Commission of Thailand <www.sec.or.th/infocenter/th/pub/headlines/lettertonation1.doc> at 20 March 2012.

²²⁹ 'SEC Proposes to Amend the Law', *Matichon* (Bangkok), 11 May 2009, 18.

²³⁰ On the contrary, the US SEC has the power to initiate a civil action on behalf of affected shareholders.

²³¹ The plaintiff is required to possess shares of such a company at the time he brings an action to the court.

²³² Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/18.

²³³ Interview with a corporate lawyer, Bangkok.

²³⁴ *Enforcement: Criminal Sanction* (2008) Securities and Exchange Commission <http://www.sec.or.th/enforcement/Content_0000000392.jsp?categoryID=CAT0000278&lang=en> at 20 March 2012.

market manipulation, insider trading, and unlicensed securities business, the Thai SEC will report the allegation to the special investigator in the Department of Special Investigation (DSI) in the Ministry of Justice.²³⁵ For other offences,²³⁶ the cases will be forwarded to the inquiry official of the Economic and Cyber-Crime Division (ECOTEC) of the Royal Thai Police. If the DSI or the ECOTEC believes that an offence has been committed, the matter will be forwarded to the Office of the Attorney General. The Office of the Attorney General will consider the case and decide whether a prosecution will be brought against the offender.²³⁷

The main criticism of the general Thai criminal prosecution system is the difficulty in prosecuting offenders under the Securities Act and relevant laws. The problems lie in the effectiveness of legal enforcement officers and Thai criminal procedural law. Fagan conducted research on these issues and interviewed members of Thai enforcement agencies and reported that police investigators and public prosecutors were not familiar with securities law.²³⁸ There has been an attempt to address the issue of the ineffectiveness of police investigators. The DSI was established in 2004 to investigate certain securities cases²³⁹ before passing the cases on to public prosecutors. During the course of interviews conducted for this thesis, an officer of the DSI explained the role of the DSI:

Our staff are from the police and the Department of Revenue, etc. The purposes of establishing the Department of Special Investigation is to have a specialised authority. One-third of us are former police. Most of us were transferred from various governmental organisations, such the Department of Revenue, about 100 persons, the Board of Investment, law schools, and the Ministry of Finance, about 150–200 persons. Now, we have approximately 700–800 staff members. We have enough personnel.

²³⁵ Stock Exchange of Thailand, *Stock Exchange of Thailand: Annual Report 2008* (2008) 51.

²³⁶ Such as an unauthorised mutual fund scheme and unlicensed derivative business operations.

²³⁷ Under the Constitution of Thailand the courts of justice are classified into three levels. They consist of the Courts of First Instance, the Courts of Appeal, and the Supreme Court. There are four specialised courts in Thailand – the Labour Court, the Tax Court, the Intellectual Property and International Court, and the Bankruptcy Court. As there is no specialised court for securities cases, a prosecution must be filed with the Courts of First Instance.

²³⁸ Fagan, above n 100, 328.

²³⁹ The special cases are the cases in which the offender possesses knowledge of and uses highly sophisticated technology in their criminal conduct, such as financial or banking fraud, computer hacking, and theft of technological trade secrets. See the Special Case Investigation Act B.E. 2547 (2004) (Thailand) s 21, Table.

Lately we have focused on training our staff to increase our capacity in dealing with special cases.²⁴⁰

However, a legal practitioner pointed out that the backgrounds of these people make them ineffective investigators:

The concept of establishment of the DSI is good and this can improve the effectiveness of law enforcement. However, practically speaking, the DSI has no specialisation in the securities area. DSI staff were transferred from other governmental departments as those staff saw no career future with their previous departments. Some cases are not properly investigated as the inspectors do not understand finance, accounting, and trading in stock market.²⁴¹

Within the Office of the Attorney General there is a separate organisation dealing with securities cases, known as the Department of Special Cases. A member of the Department explained some of the problems in the Department of Special Cases:

Our staff in the Department of Special Cases come from three groups, ie (1) the fourth grade public prosecutors who have an experience of seven or eight years. They have expertise in general cases, but not in the area of securities laws; (2) less senior public prosecutors specially used in securities cases, which is very rare; and (3) public prosecutors from the Department of Economic and Natural Resource Cases. In my opinion, the problems with the Department of Special Cases are, firstly, less senior prosecutors have to move to different departments twice a year. Due to this rotation it is impossible for us to develop prosecutors who have expertise in specific areas. Secondly prosecutors do not want to work in the Department of Special Cases because there is no incentive. This department is in charge of more and more complicated cases than other departments, without additional salary. For example, there are four public prosecutors, each from the three groups I have mentioned in my department. There are about four major cases each year but the relevant evidence is voluminous and complex. We cannot review the evidence in a timely way. The cases therefore are with us for years before being forwarded to the court. The issue of budget has not been addressed. There are not enough basic facilities provided. For example, there are not enough computers for every

²⁴⁰ Interview with an investigation authority, Bangkok.

²⁴¹ Interview with a public prosecutor, Bangkok.

prosecutor; and there is no internet connection which is required to do the necessary research.²⁴²

In addition to the lack of knowledgeable law enforcement officers, under Thai criminal procedure it is difficult for public prosecutors to secure a conviction because of the burden of proof. Violations of the Securities Act or the PLC Act are considered a crime. Public prosecutors are required to prove the offence beyond a reasonable doubt.²⁴³ As a public prosecutor pointed out:

Under criminal law the standard of proof is significantly high. The prosecutor has to prove beyond the reasonable doubt. However, in securities cases, unlike other criminal cases where it is possible to seek for evidence to prove the suspect guilty, it is hard to find evidence which clearly shows that the suspect has breached the law. There is only circumstantial evidence against wrongdoers, so it is unlikely for accused in securities cases to be convicted.²⁴⁴

Thai courts frequently dismiss securities claims on the grounds that the prosecutor's case is not sufficiently strong to prove the offence.²⁴⁵ An officer from an investigatory authority explained this issue:

In many cases, proof of guilt is unclear. Investigation normally begins long after the violation occurs. Sometimes, it is too late to collect evidence. Moreover, in some cases, evidence is usually in the possession of the accused, such as books and records. Such internal information is very difficult to access and importantly it is hard to prove how accurate the document is.²⁴⁶

A judge, interviewed for this thesis, was asked about legal enforcement and he mentioned:

My concern is the understanding of legal enforcement agencies. We do not have sufficient books and research providing knowledge for practitioners. Besides, there are no court decisions which can be used as a precedent. Consequently there is no co-understanding among us. Some mentioned that [the judges] have no sufficient

²⁴² Interview with a public prosecutor, Bangkok.

²⁴³ Criminal Procedure Code B.E. 2477 (1934) (Thailand) s 227.

²⁴⁴ Interview with a public prosecutor, Bangkok.

²⁴⁵ Securities and Exchange Commission, above n 124, 144.

²⁴⁶ Interview with an investigatory authority, Bangkok.

knowledgeable judges for securities cases. Currently we have recruited a number of judges who have expertise in securities cases. Besides if a judge has no familiarity with a special case, the prosecutors can bring an expert to give information to the court.²⁴⁷

An academic researcher also pointed out that a specialised court might not be the solution:

Regarding the courts, in Thailand there are a number of special courts dealing with special matters, which are labour, youth and family, taxation, bankruptcy, and intellectual property. Some suggest that it would be more effective if we were to have a separate court dealing with company and securities cases. I think that the establishment of a new specialised court would not make any difference. Some judges are trained for special courts and have expertise in special areas but are later moved to another court. The expertise cannot be created and retained if judges are still rotated.²⁴⁸

A case from 2005 illustrates some of the problems. A court dismissed a prosecution in which the Thai SEC believed there was fraud in financial statements. In that case, involving Picnic Corporation, the managing director reported that its net profit in 2004 had increased by about 177 per cent.²⁴⁹ In March 2005 the Thai SEC ordered Picnic to correct its financial statements.²⁵⁰ Picnic declined to do so and affirmed the accuracy of its financial statements. The Thai SEC upheld its decision and ordered Picnic to seek a special audit to clarify the company's financial status in May 2005.²⁵¹ The Thai SEC believed that Picnic had made a profit from its own capital, so filed criminal complaints with the DSI on the grounds of accounting fraud.²⁵² The DSI decided to bring a criminal action against the former Picnic executives and the other accused. Although both the

²⁴⁷ Interview with a judge, Bangkok. See also Organisation for Economic Co-operation and Development, *Corporate Governance in Asia 2011: Progress and Challenges* (2011) 30.

²⁴⁸ Interview with an academic researcher, Bangkok.

²⁴⁹ 'Revealing Picnic Transactions', *Matichon* (Bangkok), 6 June 2005, 20; Set Santi, 'Revealing the Connection between Picnic and Gas-Filling Plants', *Matichon* (Bangkok), 13 June 2005, 20; 'Picnic Transactions and the Report of the Auditor', *Matichon* (Bangkok), 29 June 2005, 20; 'Picnic Declaration to SEC – Profit from its own Money', *Matichon* (Bangkok), 27 June 2005, 20; 'From Prachachart News, Tracking Picnic's Connection', *Matichon* (Bangkok), 4 July 2005, 8.

²⁵⁰ SEC News Release No 31/2548. Nuntawun Polkuamdee, 'SEC Alleges Picnic Accounts Fraud: Shares Plummet 55% As Investors Pull Out', *Bangkok Post* (Bangkok), 1 July 2005, 1.

²⁵¹ SEC News Release No 45/2548.

²⁵² SEC News Release No 67/2548.

DSI and the Thai SEC strongly believed that Picnic had window dressed its accounts,²⁵³ the Criminal Court of First Instance found that the evidence was not sufficient to prove the defendants guilty. All Thai legal agencies and all investors questioned why criminal penalties for violations of securities law were very difficult to enforce. In the Picnic case, in particular, they queried what led to the case being dismissed: whether the investigation report prepared by the DSI was not sufficiently strong; whether the indictment submitted to the court by the public prosecutor was inconsistent with the evidence; or, whether the standard of proof in Thai criminal law is too high. In February 2007 the public prosecutor filed an appeal to the Court of Appeal.²⁵⁴ Early 2012, the Court overturned the lower court's decision and handed the 12-year imprisonment term to the defendants.²⁵⁵ This decision may shade some light on Thai legal enforcement.

3.6 Conclusion

This chapter set out the background to Thai company law and the Thai capital market in the perceived relationship between the development of Thai company law and economic development. Both economic growth and failure have had consequences for legal reform. The research then provides the background of the Thai legal system concerning minority shareholders' protection and further reviews the roles of related legal enforcement institutions. It also points out the dysfunction of the Thai legal enforcement agencies. Importantly, the findings show that the transplants of legal concepts are wholly done by Thai rulers in order to fulfil their commitments and to bring economic growth. The Thai government employs the international standard as a guideline for legal reform. The demand from the private sector for reform, however, has not been evidenced. With the absence of private demand it is questionable whether minority shareholders will benefit from reform. The minority shareholders take no part to inform the rulers of which protection they wish to have in place. The discussion on whether the

²⁵³ The SEC secretary-general insisted, '[A]ctually, the case does have sufficient evidence and we are going to explain how [manipulative] techniques have been used to dress up the accounting records. There are many details'. 'SEC to Appeal over Picnic Acquittal', *The Nation* (Bangkok), 22 December 2006, 1.

²⁵⁴ The SEC also submitted the complaint to the DSI on the allegation that two former executives of Picnic, with the assistance of three associated persons, funnelled the money out of the company for their own benefit through the creation of several fraud-buying transactions and falsified the company's books and records purporting to defraud others in October 2006. Securities and Exchange Commission, *Stock Exchange of Thailand: Annual Report 2006* (2006) 71–2.

²⁵⁵ 'Executives Get 12-year Prison Terms', *Bangkok Post* (Bangkok), 23 February 2012.

adopted rules can effectively protect minority shareholders' interests is in the following chapters. From the next chapters the research focuses on the comparative study of laws and regulations on minority shareholders' protection in the US, Germany, and Thailand in different aspects. The next chapter discusses the fundamental rights provided to minority shareholders in the three jurisdictions.

Chapter 4

The Fundamental Rights of Minority Shareholders

- 4.1 Introduction
- 4.2 Shareholders' management rights
 - 4.2.1 Shareholders' participation in shareholders' meetings
 - 4.2.1.1 The right to obtain information on the agendas to be voted
 - 4.2.1.2 The right to vote *in absentia*
 - 4.2.1.3 The right to propose an agenda
 - 4.2.2 Shareholders' participation in the appointment of board members
 - 4.2.2.1 Cumulative voting
 - 4.2.2.2 Nomination process
 - 4.2.2.3 Independent directors
- 4.3 Proprietary rights of shareholders
 - 4.3.1 Maintaining the shareholding
 - 4.3.2 Rights to dividends
- 4.4 Conclusion

4.1 Introduction

The previous chapters provided the background to the research and reviewed the relevant literature which led to the research questions. As one of the research questions considers how the Thai legal framework protects minority shareholders, the following chapters compare Thai law with United States and German law. This chapter outlines the fundamental rights of minority shareholders in these three legal systems of corporate law.

In a widely diffused company, according to Berle and Means, individual shareholders have no control over the company because, given their small stake, the decision-making has shifted away to the managers.¹ Similarly, in a concentrated ownership company, minority shareholders have no control as in company a majority of the shares are held by controlling shareholders.² Both situations, minority shareholders have no power over

¹ See Adolf A Berle Jr and Gardiner C Means, *The Modern Corporation and Private Property* (1933).

² See Rafael La Porta, Florencio Lopez-de-Silanes and Andrei Shleifer, 'Corporate Ownership Around the World' (1999) 54(2) *The Journal of Finance* 471.

the company, it is necessary to observe the fundamental rights they have and how they can exercise them in order to protect their investment. This chapter surveys legal frameworks governing two categories of shareholders' rights in US, German, and Thai law: management rights and proprietary rights. The chapter covers: firstly, shareholders' rights in decision making at the shareholders' meetings; secondly, the shareholders' participation in the appointment of board members; and, thirdly, shareholders' proprietary rights.

4.2 Shareholders' management rights

In the US and Thailand, the significant organs of a company are the board of directors and the shareholders' general meeting. In Germany, as mentioned in Chapter 2, the core organs are the management board, the supervisory board, and the shareholders' meeting. In both board structures the board of directors, or the management board, is empowered to represent the company in dealing with third parties. The power of management, according to the company's constitution, is solely granted to the board. The shareholders in a general meeting, or the supervisory board, cannot usurp such power, and *vice versa*.³ Due to the limited power of shareholders, the law should protect their rights and facilitate their exercise. This section considers the rights of shareholders to participate in management in two ways: in the shareholders' meetings, and, in the appointment of board members.

4.2.1 Shareholders' participation in shareholders' meetings

The shareholders' meeting is significant as it is the venue where all shareholders may vote on important issues, such as the appointment of board members and the amendment of the company's articles of association. Although minority shareholders have voting rights, it is questionable whether such rights, in particular, can be effectively exercised by them.⁴ The issues to be discussed in the shareholders' meetings

³ See Ian M Ramsay and Harold Arthur John Ford, *Ford's Principles of Corporation Law* (12th ed, 2005) 212.

⁴ Buxbaum and Hopt argued that the role of the general shareholders' meeting was unclear. It seemed necessary for exceptional circumstances but this was a mere formality so could be left without harm. See Richard M Buxbaum and Klaus J Hopt, *Legal Harmonization and the Business Enterprise* (1988) 181–2.

are generally set by the management. The management may push only issues that they wish and ignore other matters, particularly those relating to the company's poor performance. In concentrated ownership companies, controlling shareholders may use the shareholders' meetings to pass resolutions in which they have a related interest. Given these circumstances, this section considers how relevant laws in the US, Germany and Thailand ensure the rights of minority shareholders to effectively participate in the meeting. It considers three issues: (i) whether the shareholders receive sufficient information relating to the agendas to be voted on; (ii) whether the shareholders can vote without their physical attendance; and, (iii) whether the shareholders have the right to propose an issue to be considered at the meeting.

4.2.1.1 The right to obtain information on the agendas to be voted

The notice of the meeting is considered to be an important document because it provides the details of the meeting and relevant information assisting shareholders to understand the issues to be discussed. Two aspects are significant: (i) the information provided with the notice, and (ii) the length of time. The notice should contain the details of the location of the meeting, the agenda, and all relevant information necessary for shareholders to consider before voting. A period of minimum notice is necessary to enable shareholders to consider the materials, communicate among themselves, and make their decisions.

The Delaware General Corporation Law ("DGCL") Section 222 specifies that a meeting of the company is to be convened by notice in writing that includes the details of place, date and hour of the meeting, the voting process, and the purposes of the meeting. Such notice to shareholders must be given not less than 10 or more than 60 days before the date of the meeting.⁵ The notice must be mailed directly to the shareholders at their addresses as they appear in the corporation's records.⁶ For companies listed on the New York Stock Exchange, the requirement of at least 10 days notice is imposed.⁷ In Germany, the *Aktiengesetz* of 2009 [Stock Corporation Act] ("*AktG*") provides that the

⁵ Delaware General Corporation Law § 222(1).

⁶ Ibid § 222(2).

⁷ NYSE Amex Company Guide §§ 701–2.

notice of the shareholders' meeting must include the time and place of the meeting and the procedure for voting.⁸ The law requires the notice to be given to shareholders not later than 30 days prior to the meeting date.⁹ In addition, companies are required to publish the notice of the meeting in the company's designated journals and the Electronic Federal Gazette (*elektronischer Bundesanzeiger*).¹⁰ In Thailand, under the Public Limited Company Act, the notice of the meeting must include the date, the time, the agenda, and any relevant opinions of the board of directors.¹¹ The notice must be given to shareholders not less than seven days before the date of the meeting.¹² Companies are also required to announce the details of the meeting in a newspaper not less than three days prior to the meeting.¹³

In all, corporate laws in the three jurisdictions attempt to ensure the adequacy of information of the meeting, safe receipt of the notices by shareholders, and sufficient time for shareholders to prepare for the meeting. The length of the required notice of the meeting in the three jurisdictions is different. Of the three jurisdictions, Thai law provides the shortest notice for shareholders but it requires the company to publish the notice of the meeting in a newspaper.

4.2.1.2 The right to vote *in absentia*

To ensure the right of shareholders to participate in voting at shareholders' meetings, the law should provide a means for shareholders to vote their shares even when they are unable to attend. This section considers whether shareholders are able to vote *in absentia*; and how the law in the US, Germany and Thailand protects shareholders when proxies are solicited.

⁸ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 121(3).

⁹ *Ibid* § 123(1).

¹⁰ *Ibid* §§ 25, 121(3).

¹¹ Public Limited Company Act B.E. 2535 (1992) (Thailand) s 101.

¹² *Ibid*. In some matter such as mergers, asset acquisitions and delisting, 14-day notice is required. The detail on these issues is discussed in Chapter 6.

¹³ *Ibid*.

Proxy voting

Under Section 215 of DGCL, shareholders are entitled to vote by proxy. The proxy granted is effective for three years unless a longer period is specified. The use of proxy voting is very common in practice. German practice is significantly different from that of the US. Baums explained:

As most shares in public limited companies are held in bearer form, the by-laws of the company may provide that the right to participate and vote at the meeting can only be if the shares have been deposited with a notary public, a depositary bank or the company itself not longer than ten days before the meeting.¹⁴

To vote, shareholders must either attend the meeting in person or give a proxy to a representative.¹⁵ The proxy form must be in writing and be submitted to the company.¹⁶ Unlike US, shareholders rarely give proxies.¹⁷ In practice, as noted in Chapter 2, shareholders often deposit their shares with custodian banks. The banks can exercise voting rights only to the extent that a shareholder has given express instructions.¹⁸ If no instructions are given, banks may exercise any voting rights in three ways: according to their own proposals or the proposal of the management board or that of the supervisory board.¹⁹ If the banks wish to exercise their rights on the basis of their own proposals, they must inform the shareholders of this.²⁰ The banks must also ensure that the interests of themselves and the shareholders are considered.²¹ The law requires that the bank must inform the shareholders that if no instruction is given they will exercise the voting right in accordance with their own interests.²² In practice, shareholders are unlikely to give any instructions to the custodian banks.²³ Apart from holding the shares

¹⁴ Theodor Baums, 'Shareholder Representation and Proxy Voting in the European Union: A Comparative Study' (Paper presented at the Comparative Corporate Governance, Hamburg, Germany, 15–17 May 1997) 11.

¹⁵ § 134(3) of *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) permits proxy voting.

¹⁶ *Ibid.*

¹⁷ Braendle viewed that in practice the proxy authorising the company to exercise shareholders' voting rights in Germany was 'alien'. Udo C Braendle, 'Shareholder Protection in the USA and Germany – "Law and Finance" Revisited' (2006) 7(3) *German Law Journal* 257, 267.

¹⁸ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 135(1).

¹⁹ *Ibid.*

²⁰ *Ibid* § 135(2).

²¹ *Ibid.*

²² *Ibid.*

²³ Theodor Baums, 'Corporate Governance in Germany: The Role of the Banks' (1992) 40 *The American Journal of Comparative Law* 503, 506.

of their customers, German banks may also own shares in their own right. The *AktG* requires the banks to inform the shareholders of this as well.²⁴

In Thailand, proxy voting is also permissible and is more like US practice.²⁵ The proxy must be in writing containing the details of the shares authorised to be voted, the name of the proxy holder, and the serial number of the meeting that the proxy holder is authorised to attend and vote.²⁶ The proxy must be submitted to the chair of the board or to the person assigned by the chair.²⁷

In conclusion, proxy voting is permissible in the three jurisdictions. Shareholders in German companies, unlike those in US and Thai companies normally deposit their shares to banks and authorise them to exercise voting rights and this leads to some variations between German, US, and Thai law and practice.

Proxy solicitation

The concept of proxy solicitation is closely related to the agency relationships found in corporate law.²⁸ A proxy holder is authorised to vote on behalf of a shareholder on the issues on which a shareholder has a right to vote.

In the US, prior to a meeting to approve important resolutions, such as the election of directors nominated by the management, appointment of auditors, or directors' remuneration, the management attempts to solicit proxies from shareholders to vote for its proposal. In the US, as noted in Chapter 2, a rule on proxy solicitation first appeared in the Securities Exchange Act of 1934 ("Exchange Act") to ensure that the shareholders are fully informed of all matters on which they are asked to vote at the shareholders' meeting.²⁹ In 1992 the proxy rules were revised to allow greater

²⁴ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 135(2), (3).

²⁵ Public Limited Company Act B.E. 2535 (1992) (Thailand) s 102.

²⁶ *Ibid* ss 34, 102.

²⁷ *Ibid* s 102.

²⁸ Arthur R Pinto and Douglas M Branson, *Understanding Corporate Law* (2nd ed, 2004) 165.

²⁹ Jeffrey Bauman, Elliott Weiss and Alan Palmiter, *Corporations Law and Policy: Materials and Problems* (5th ed, 2003) 480–1.

communication among minority shareholders.³⁰ Proxy solicitation was further addressed during the 1990s while takeover transactions were prevalent.³¹ In these contests, the management of potential target companies uses techniques, such as the poison pill and golden parachutes, to prevent hostile takeovers. On the other hand, the acquiring company attempts to acquire sufficient shareholders' votes to install new directors. These conflicts are known as "proxy contests" or "proxy fights".³²

The proxy rules are applied to: (1) companies whose securities are traded in the stock market, or (2) companies that have total assets exceeding US\$10 million and a class of equity security held by 750 or more persons.³³ To solicit proxies from shareholders, the management is required to follow Regulation 14A made under the Exchange Act. Rule 14A specifies the detailed information to be furnished to security holders,³⁴ the form of the proxy,³⁵ the proxy statement,³⁶ and the requirement on filing preliminary copies of the proxy statement and the form of a proxy with the SEC, etc.³⁷ Apart from the management, the Exchange Act also allows a shareholder to acquire other shareholders' proxies.³⁸ Shareholders may request the company to mail their soliciting materials to other shareholders if they agree to bear the cost of postage.³⁹ The company is required to provide the shareholders with an updated list of names and addresses of shareholders that they require.⁴⁰ Furthermore, to ensure that the information submitted to shareholders is accurate, all delivered documents must not include any false or misleading statements.⁴¹ Some weeks before the annual meeting, shareholders in US corporations receive a large pack containing an annual report for the previous year, the management's discussion and analysis of the previous year, and the financial

³⁰ Ibid.

³¹ See, eg, Nell Minow, 'Proxy Reform: The Case for Increased Shareholder Communication' (1991–1992) 17 *Journal of Corporation Law* 149; Carol Goforth, 'Proxy Reform as a Means of Increasing Shareholder Participation in Corporate Governance: Too Little, but not Too Late' (1993–1994) 43 *American University Law Review* 379.

³² Pinto and Branson, above n 28, 168–9.

³³ Securities Exchange Act of 1934 §§ 12, 12(g-1).

³⁴ Ibid Rule 14a-3.

³⁵ Ibid Rule 14a-4.

³⁶ Ibid Rule 14a-5.

³⁷ Ibid Rule 14a-6.

³⁸ Ibid Rule 14a-7.

³⁹ Ibid Rule 14a-7(a),(e).

⁴⁰ Ibid Rule 14a-7(a).

⁴¹ Ibid Rule 14a-9.

statements.⁴² A proxy statement is included to inform shareholders of the details of the issues to be voted on at the meeting. Importantly, shareholders will get proxy cards enabling them to express their opinions on the management's proposals. If they choose to grant proxies, they sign and return the cards in the enclosed envelope to the corporation or proxy-soliciting firm.

Unlike the US, proxy solicitation is not common in Germany. According to Baums, 'there is no proxy statement similar to that in the US'.⁴³ If shareholders of German corporations wish to vote, they have to attend the meeting in person or authorise proxy holders to act on their behalf.⁴⁴ In practice, shareholders prefer to hold their shares in a bearer form although a registered form is also available. To transfer a bearer share, an endorsement by its owner is not required as an agreement and a delivery of the certificate are sufficient.⁴⁵ Consequently, most shareholders tend to deposit their shares with the banks for safety reasons.⁴⁶ Furthermore, all share transfers are subject to tax except for transfers between customers of the same bank as the bank is still recorded as the holder.⁴⁷ Due to these practices, most German banks offer custodian services that include share depository and voting on behalf of their clients.⁴⁸ The role of banks in acting on behalf of shareholders is acknowledged in German corporate law.⁴⁹ At least 21 days prior to the meeting a company is required to submit the notice of the meeting, the agendas and any motions or nominations made by shareholders, as well as any

⁴² Pinto and Branson, above n 28, 166.

⁴³ Baums, above n 14, 11.

⁴⁴ Ibid.

⁴⁵ Bernd Singhof and Oliver Seiler, 'Shareholder Participation in Corporate Decisionmaking Under German Law: A Comparative Analysis' (1998) 24 *Brooklyn Journal of International Law* 493, 507–8.

⁴⁶ Jean J Du Plessis and Claus Luttermann, 'The Dominant Role of the German Banks' in Jean J Du Plessis et al (eds), *German Corporate Governance in International and European Context* (2007) 206–7.

⁴⁷ Mark J Roe, 'Some Differences in Corporate Structure in Germany, Japan, and the United States' (1992–1993) 102 *The Yale Law Journal* 1927, 1971; John C Coffee Jr, 'The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control' (2001) 111 *The Yale Law Journal* 1, 53.

⁴⁸ Singhof and Seiler, above n 45, 508.

⁴⁹ For a detailed study on the role of German banks, see Section 2.3.2. For a discussion on the relationship between banks and the supervisory board, see, eg, Theodor Baums, 'Corporate Governance in Germany: The Role of the Banks' (1992) 40 *The American Journal of Comparative Law* 503; Peter O Mühlbert, 'Bank Equity Holding in Non-Financial Firms and Corporate Governance' in Klaus J Hopt et al (eds), *Comparative Corporate Governance: The State of the Art and Emerging Research* (1998); Ekkehard Wenger and Christoph Kaserer, 'German Banks and Corporate Governance: A Critical View' in Klaus J Hopt et al (eds), *Comparative Corporate Governance: The State of the Art and Emerging Research* (1998).

management proposals to the custodian banks.⁵⁰ The law further requires the banks to promptly forward any documents received from the company to shareholders whose shares are in their custody.⁵¹

In Thailand, the regulation of proxies, together with other changes such as shareholders' proposals, was introduced in 2008 with the aim of Thai company law reflecting international standards.⁵² The purpose of proxy regulation is to ensure that shareholders must receive accurate information before giving their proxies.⁵³ Section 89/31 of the Securities and Exchange Act ("Securities Act") defines the meaning of solicitation as a communication to the shareholders of a company with the intent of enticing the shareholders to give a proxy to the person communicating or any other persons to attend and vote at the shareholders' meeting on their behalf. It further authorises the Capital Market Supervisory Board to make further rules, conditions, and procedures regarding proxy solicitation.⁵⁴

The above survey reveals that, as indicated, the appointment of proxies is possible in the three jurisdictions. German practice is markedly different from that of the US and Thailand. In Germany, proxy solicitation is not necessary as most small shareholders are represented by custodian banks. The policies underlying proxy solicitation in the US and Thailand are similar – the intention is to protect shareholders from deceptive solicitations. It is believed that this may facilitate shareholders in counterbalancing the management's powers. The research shows that, in the US, proxy solicitation is widely used because given the diffused ownership structure it is possible for minority shareholders to exercise some control over management. The law seeks to ensure that proxy solicitation is transparent and that fraudulent misleading behaviour is minimised. On the other hand, Thai companies are mainly controlled by large shareholders. It would be rare for minority shareholders to acquire sufficient votes to overcome that

⁵⁰ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 125(1).

⁵¹ *Ibid* § 128(1).

⁵² The enactment of the Securities and Exchange Act (No 4) B.E.2551 (2008) (Thailand).

⁵³ Information based on an interview with an officer of the Thai SEC, Bangkok.

⁵⁴ The Thai SEC is in the process of drafting regulations governing proxy solicitation. The hearing on draft regulations was taken in June 2008. SEC News No 37/2008. Until now, the draft regulations have not come into effect.

control.⁵⁵ As a result, proxy solicitations to install a new management, a “proxy contest”, do not happen.⁵⁶ In practice, the adoption of proxy solicitation has unlikely to benefit minority shareholders.

4.2.1.3 The right to propose an agenda

Generally, the issues to be discussed in the shareholders’ meetings are proposed by the management. Although shareholders have the right to vote in their meetings, they will vote only on the matters set by the board. To allow shareholders to take part in management, they should have an opportunity to propose a matter to be considered by their fellows in the meeting. All three jurisdictions have similar principles reflected in their law with the US having the most detailed procedural provisions.

Influenced by the study of Berle and Means, which revealed the difficulties for shareholders of the US listed companies to influence the board, the US Congress introduced shareholders’ proposals in the Exchange Act to provide a mechanism for them to control the management and take part in corporate decision-making.⁵⁷ Only a shareholder who continuously holds shares with a market value of at least US\$2,000 or at least one per cent of the shares for at least one year is entitled to submit a proposal.⁵⁸ The shares must be held at the date of the meeting.⁵⁹ The law limits each qualified shareholder to one proposal.⁶⁰ Also, the proposal, including any supporting statement, must not exceed 500 words.⁶¹ The shareholder is required to submit the proposal to the company’s principal executive officer not less than 120 calendar days before the date of the company’s proxy statements are released to shareholders in the previous year’s annual meeting.⁶² The company will then decide whether to place it on the company’s proxy statement or omit a proposal. In a case of omission, Rule 14-a requires the company to submit its reasons for exclusion to the Securities and Exchange

⁵⁵ Information based on interviews with corporate lawyers, Bangkok.

⁵⁶ Ibid.

⁵⁷ Daniel E Lazaroff, 'Promoting Corporate Democracy and Social Responsibility: The Need to Reform the Federal Proxy Rules on Shareholder Proposals' (1997–1998) 50 *Rutgers Law Review* 33, 36.

⁵⁸ Securities Exchange Act of 1934 Rule 14a-8 Question 2.

⁵⁹ Ibid.

⁶⁰ Ibid Question 3.

⁶¹ Ibid Question 4.

⁶² Ibid Question 5.

Commission (“SEC”).⁶³ A dissenting shareholder may submit his own statement to the SEC responding to the company’s arguments.⁶⁴ If the proposal is placed on the company’s proxy statement, the company may insert the reasons why it believes shareholders should vote against the proposal.⁶⁵ The proposing shareholder is required to attend the meeting to present his proposal. Otherwise the company is authorised to exclude all proposals submitted by the shareholder from its proxy materials for any meetings in the following two calendar years.⁶⁶

In German corporations a shareholder may respond to what the board of directors has proposed in two different ways. Firstly, a shareholder may request the management to place additional issues on the agendas. The eligible shareholders are those whose shares together reach at least five per cent of share capital or the proportional amount of €500,000.⁶⁷ Such shareholders must also continuously have been in possession of the shares for at least three months prior to the demand being filed.⁶⁸ The demand must be submitted to the company at least 30 days prior to the meeting.⁶⁹ The company must publish the additional agenda items together with the notice of the meeting in the Electronic Federal Gazette immediately following the receipt of the request.⁷⁰ The shareholder who proposes the additional agenda item must hold shares at the date of the meeting.⁷¹ Secondly, the shareholder may submit a counter-motion to oppose any proposal of the management or the supervisory board. A counter-motion must state the grounds of such a motion and reach the company no later than 14 days prior to the meeting.⁷² The length of a counter-motion is limited to 5,000 characters.⁷³ The company must publish the counter-motion on the company’s internet page.⁷⁴ The management is allowed not to publish the shareholder’s counter-motion under specific

⁶³ Ibid Question 9–10.

⁶⁴ Ibid Question 11.

⁶⁵ Ibid Question 13. The company is required to send the shareholder a copy of its statement before distributing to all shareholders. The shareholder may submit another statement clearly explaining the reasons for their views or the information demonstrating the inaccuracy of the company’s claims.

⁶⁶ Ibid Question 8.

⁶⁷ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 122(2).

⁶⁸ Ibid §§ 122(2), 142(2).

⁶⁹ Ibid § 122(2).

⁷⁰ Ibid § 124(1).

⁷¹ Ibid § 142(2).

⁷² Ibid § 126(1).

⁷³ Ibid § 126(2).

⁷⁴ Ibid § 126(1).

circumstances. For example, if the motion is to make the shareholders' meeting illegal; the motion contains false or misleading statements; or, the matters mentioned in the counter-motion are based on facts already communicated.⁷⁵ The shareholder who proposes the counter-motion is required to attend the meeting.⁷⁶

Similarly to German law, shareholders in Thai listed companies with at least five per cent of the total voting rights are able to request the board of directors to include a matter as an agenda item at the shareholders' meeting.⁷⁷ The proposal must indicate whether it is for consideration or for approval. The board may not include the matter proposed by a shareholder if it is found to be: not in compliance with the requirements of, nor relevant to, ordinary business operations; beyond the company's power to produce the proposed result; or, identical to an issue proposed in the previous 12 months which did not receive the support of more than 10 per cent of the voting rights.⁷⁸ The Securities Act authorises the Capital Market Supervisory Board to make additional rules relating to shareholders proposals, including the grounds for a board to not include a proposal on the agenda.⁷⁹ If the board refuses to include the matters proposed by the shareholder in the agenda, it is obliged to explain the reasons for such a refusal to the meeting.⁸⁰ A matter rejected by the board may be included on the agenda for a meeting if the shareholders with a majority vote of the total number of the shareholders present at the meeting agree to its inclusion.⁸¹

In the interviews conducted for this thesis, an officer of the Thai SEC explained that this rule aimed to provide an additional right to qualified shareholders.⁸² This was also to ensure that the corporate governance of Thai companies met international standards.⁸³ However, another interviewee remarked that, despite the additional right provided,

⁷⁵ Ibid § 126(2).

⁷⁶ Ibid § 126(2).

⁷⁷ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/28 paragraph 1.

⁷⁸ Ibid s 89/28 paragraph 2.

⁷⁹ Ibid s 89/28 paragraph 2(5). The Capital Market Supervisory Board has not announced any rule on this issue.

⁸⁰ Ibid s 89/28 paragraph 3.

⁸¹ Ibid s 89/28 paragraph 4.

⁸² Interview with an official from the Thai SEC, Bangkok.

⁸³ Ibid.

minority shareholders rarely exercised it.⁸⁴ Some interviewees agreed that minority shareholders did not see their stake in the company as sufficiently significant to attempt to push issues through the meeting; they therefore might not see the advantage of this new rule to them.⁸⁵ A corporate lawyer stated:

Shareholder proposals have never happened and are unlikely to happen because of the nature of Thai minority shareholders. Most of them are not investors but speculators. They do not pay sufficient attention to their shares and rights. For example, they have no interest to attend meetings or [if attending] to participate. Some shareholders attend the meeting merely to receive some gifts given by the company. Giving away gifts is done to gain the attendance of a sufficient number of small shareholders in order to meet the quorum requirement.⁸⁶

Overall, minority shareholders in the three jurisdictions have the right to submit a shareholder proposal to be included in the business to be considered at a shareholders' meeting. The details of those rights vary. Firstly, both Delaware and German laws stipulate an ownership requirement that an eligible shareholder must continually hold shares for at least a year and three months respectively and hold shares at the time of the shareholders' meeting. However, similar requirements do not exist in Thai law. Without these requirements, this process may be abused. Secondly, it is difficult for Thai minority shareholders to submit a proposal as proposing shareholders must hold at least five per cent of the company's shares. Five per cent of the average capitalisation of a company in the SET50 is approximately 6,591 million baht.⁸⁷ It is unlikely for individual Thai minority shareholders to hold shares of this value. In addition, unlike German law that provides an electronic shareholders' forum, there is no affordable and timely mechanism facilitating small shareholders' communication with each other to collect the percentage of shares required. Finally, the findings show that although this legal concept could benefit minority shareholders, Thai minority shareholders may not see it as a significant advantage to them.

⁸⁴ Interview with an official from the Thai SEC, Bangkok.

⁸⁵ Interviews with a professional independent director and an investor, Bangkok.

⁸⁶ Interview with a corporate lawyer, Bangkok.

⁸⁷ The capitalisation of the SET50 is 6,591,087.41 million baht. *Market Statistics* (2012) The Stock Exchange of Thailand <http://www.set.or.th/en/market/market_statistics.html> at 20 March 2012.

4.2.2 Shareholders' participation in the appointment of board members

As already observed, the board of directors, or the management board in the German context, is empowered to operate the day-to-day business of the company and to make decisions regarding the company's business within the scope allowed. Shareholders have no power to disallow decisions made within the authorised scope of the board's power. Given the power of the board, the process of appointing board members is very important. This section considers: firstly, how the laws in the three jurisdictions provide mechanisms allowing minority shareholders to participate in appointing board members; and secondly, who has the effective power to appoint the board members. The second question is a significant issue because, as mentioned in Chapter 2, the ownership of Thai companies is concentrated in the hands of controlling shareholders. Controlling shareholders may use their voting power to elect their non-qualified acquaintances to sit on the board. There are three significant issues to be considered: cumulative voting, nomination committee, and independent directors.

4.2.2.1 Cumulative voting

Under straight voting, in which each shareholder can vote all of their shares for each position, shareholders holding a majority of the company's shares are able to elect all the members of the board. Consequently company law should require a process to allow minority shareholders to elect representatives onto the board. Under DGCL, there is a voting procedure known as cumulative voting, facilitating minority shareholders to cast all of their votes, the number of their stocks multiplied by the number of the directors to be elected, for a single candidate.⁸⁸ In practice, only a couple of states in the US make

⁸⁸ Delaware General Corporation Law § 216. For example, if shareholder One has 70 shares while shareholder Two has 30 shares in an election for three directors, shareholder One will have 210 votes (70 x 3) and shareholder Two will have 90 votes (30 x 3). Shareholder One wishes to elect A, B, and C as directors while shareholder Two wishes to elect X, Y, and Z. In a straight vote, shareholder A would be able to elect A, B, and C, and no candidate voted for by shareholder Two would be on the board. However, under cumulative voting, if shareholder A votes equally for A, B, and C, each will receive 70 votes. As shareholder Two has 90 votes, if all are cast for one of either X, Y, or Z, at least one will be elected to the board.

cumulative voting mandatory⁸⁹ and it is not commonly used in publicly held corporations.⁹⁰

Shareholders in a German company cannot directly elect the board of management. They instead elect supervisory board members⁹¹ at a shareholders' annual meeting,⁹² then the supervisory board appoints the members of the management board.⁹³ Kraakman argued that cumulative voting was unknown in German company law.⁹⁴ Braendle, however, pointed out that there was a similar voting procedure that may provide the same protection for minority shareholders.⁹⁵ The *AktG* specifies that the articles of incorporation may allow certain shareholders to elect up to one-third of the shareholders' representatives on the supervisory board.⁹⁶ This may permit particular shareholders, including minority shareholders, to have the special right to appoint one or more members of the supervisory board. German public companies generally apply the straight voting system in electing the supervisory board.⁹⁷

In Thailand, a method of cumulative voting, similar to the US practice, is recognised.⁹⁸ It is not compulsory; therefore, in practice, almost all Thai firms opt out of this rule in their articles of association.⁹⁹ During an interview with a regulator, the researcher asked him whether cumulative voting should be compulsory for listed companies. The regulator stated that:

Even though in theory [cumulative voting] benefits minority shareholders, forcing listed companies to comply with cumulative voting procedures may discourage companies from listing as this voting procedure had a significant effect on the voting power of the

⁸⁹ Reinier Kraakman et al, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2004) 55. For details on the debate on cumulative voting, see Sanjai Bhagat and James A Brickley, 'Cumulative Voting: The Value of Minority Shareholder Voting Rights' (1984) 27 *The Journal of Law and Economics* 339.

⁹⁰ Pinto and Branson, above n 28, 109.

⁹¹ The supervisory board consists of the representatives of the shareholders and the employees equally. For details of the supervisory board, see Chapter 2.

⁹² *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 101(1).

⁹³ *Ibid* §§ 84, 101(1).

⁹⁴ Kraakman et al, above n 89, 55.

⁹⁵ Braendle, above n 17, 271.

⁹⁶ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 101(2).

⁹⁷ Bernhard von Falkenhausen and Ernst C Steefel, 'Shareholders' Rights in German Corporations (AG and GmbH)' (1961) 10(4) *The American Journal of Comparative Law* 407, 413–4.

⁹⁸ Public Limited Companies Act B.E. 2535 (1992) (Thailand) s 70, paragraph 1.

⁹⁹ Based on the interview with a corporate lawyer, Bangkok.

controlling shareholder. Given the limited number of listed companies in the Thai stock market, lifting the burden on listed companies must be carefully considered.¹⁰⁰

The cumulative voting in theory benefits minority shareholders but, in all three jurisdictions, it is not used in practice.

4.2.2.2 Nomination process

The nomination process for directors potentially benefits minority shareholders as, although they have no sufficient voting power to elect their delegates, it provides a guarantee that the candidates of board members are chosen by independent committees. This section outlines the nomination process in the three jurisdictions. This is to illustrate how minority shareholders participate and whether the nomination process is transparent.

In the US, the concept of a nominating committee was recommended by the American Law Institute in 1994.¹⁰¹ Publicly held corporations were advised to set up a nominating committee to identify candidates suitable for election to the board.¹⁰² The rules regarding nominating committees were not in state corporation law but in the listing rules of the respective stock exchanges. At the beginning, establishing a nominating committee was voluntary and the role of the committee was unclear.¹⁰³ In practice, nominating committees had about five members, consisting of one insider (generally the Chief Executive Officer (“CEO”)) and four outsiders.¹⁰⁴ Later, the listing rules were significantly changed. They require a listed company to have a nominating committee composed entirely of independent directors.¹⁰⁵ This is to ensure that the committee will not be influenced by the CEO.¹⁰⁶ The main functions of the committee are to identify

¹⁰⁰ Interview with a regulator, Bangkok.

¹⁰¹ American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations* (1994) Part III.

¹⁰² ALI Principles of Corporate Governance § 3A.04.

¹⁰³ 'Session Three: Board Committees' (1984) 6(3) *Journal of Comparative Business and Capital Market Law* 231, 236.

¹⁰⁴ Ibid.

¹⁰⁵ NYSE's Listed Company Manual s 303A.04(a).

¹⁰⁶ Bauman, Weiss, and Palmiter, above n 29, 584.

and to recommend to the shareholders' meeting individuals qualified to be board members consistent with criteria approved by the board.¹⁰⁷

In Germany, it is recommended that listed companies have the nomination committee to elect members of the supervisory board.¹⁰⁸ The election of the management board, as discussed in Chapter 2, is within the sole power of the supervisory board. Section 5.3.3 of the *German Corporate Governance Code* states that the supervisory board must constitute a nomination committee to propose suitable candidates to the supervisory board. The supervisory board then recommends the candidates to the shareholders' meeting. Lieder pointed out that this is to make the supervisory board more autonomous and to allow the supervisory board to make a decision without the influence of the management board.¹⁰⁹ The Code further recommends the nomination committee to be composed exclusively of shareholder representatives.¹¹⁰ The Code does not empower labour representatives to take part in the nomination committee because, as indicated in Chapter 2, the *Mitbestimmungsgesetz* of 1976 [Co-determination Act] already specifies the number of labour seats on the supervisory board. In practice, almost all of the 30 largest listed companies comply with this recommendation.¹¹¹

The *Code of Good Corporate Governance* established by the Stock Exchange of Thailand has also adopted the concept of nomination committees. It resulted from the report conducted by the World Bank in 2005 that suggested Thailand considers requiring a nomination committee for listed companies.¹¹² In practice, large Thai listed companies follow this recommendation.¹¹³ The Code recommends that all listed companies constitute a nomination committee according to the criteria and processes for nominating board members, to select qualified candidates according to that criteria, and,

¹⁰⁷ NYSE's Listed Company Manual s 303A.04(b).

¹⁰⁸ For details on the nomination process of the supervisory board, see David Donald, 'The Nomination of Directors under US and German Law' (Working Paper Series No 21, Institute for Law and Finance, 2005).

¹⁰⁹ Jan Lieder, 'The German Supervisory Board on its Way to Professionalism' (2010) 11 *German Law Journal* 115, 141–2.

¹¹⁰ German Code of Corporate Governance s 5.3.3.

¹¹¹ Lieder, above n 109, 141.

¹¹² World Bank, *Report on the Observance of Standards and Codes (ROSC): Corporate Governance Country Assessment: Thailand* (World Bank, 2005) v.

¹¹³ Information based on the interviews with a professional independent director and an investor, Bangkok.

to recommend the nominated candidates to the board.¹¹⁴ The board formally recommends them to the shareholders' meeting. The members of the nomination committee are appointed by the board of directors. The majority of its members should be independent directors¹¹⁵ to ensure that the nomination committee can function transparently and independently.¹¹⁶

Overall, the concept of the nomination committee is acknowledged in the three jurisdictions. Its main function is to recommend suitable candidates to be appointed by the shareholders in the meeting. In the US, listed companies are required to establish such a committee. In Germany and Thailand, it is voluntary. In practice, German and Thai listed companies follow this recommendation. Both rules and practices applied in the three jurisdictions focus on the independence of the nomination committees.

4.2.2.3 Independent directors

Adam Smith recognised the agency problem with directors, that directors would not be as efficient in the management of the shareholders' capital as the shareholders themselves.¹¹⁷ Jensen and Meckling more recently developed agency theory to explain the conflicts of interest between directors and shareholders.¹¹⁸ The members of the board may be more concerned with their own interests instead of maximising the benefits for shareholders – their principals. To reduce such conflicts, made worse by the separation of ownership and control, different processes have been suggested. Some seek to reconcile the divergence between the interests of the principals and the agents. Others aim to ensure an effective monitoring system. One mechanism to facilitate better monitoring is the use of outsiders on the board of directors to evaluate management performance, provide recommendations, and to protect the interests of all

¹¹⁴ Stock Exchange of Thailand, *The Principles of Good Corporate Governance for Listed Companies* (2006) Principle V 2.1.

¹¹⁵ Corporate Governance Center, *Nomination Committee Guidelines* (2008) Stock Exchange of Thailand <<http://www.set.or.th/en/regulations/cg/files/NCEngforPublishing.pdf>> at 20 March 2012; Stock Exchange of Thailand, *The Principles of Good Corporate Governance for Listed Companies*, Principle V 2.2.

¹¹⁶ Stock Exchange of Thailand, above n 115, Principle V 2.2.

¹¹⁷ Adam Smith, *Wealth of Nations* (1776) 700.

¹¹⁸ For details on the agency theory, see Chapter 2.

shareholders.¹¹⁹ This section considers Delaware, German and Thai laws and regulatory practices in ensuring that the board of directors has members with no substantial relationship with controlling shareholders or existing board members.

In the US, all companies listed on the NYSE are required to have a majority of independent directors.¹²⁰ The NYSE listing rules specify the qualifications of an independent director.¹²¹ Firstly, the board of directors is required to affirm that independent directors have no material relationship with the company.¹²² This includes commercial, industrial, banking, consulting, legal, accounting, and familial relationships. Some specific relationships exclude a person from being an independent director: current employees; former employees within the last three years; partners or employees of the company's auditor during the past three years; an employee of a company that has made payments to, or received payments from the company for property or services in an amount exceeding US\$1, or two per cent of the company's consolidated gross revenues within the last three years.¹²³ Immediate family members of these people are also excluded.¹²⁴ The Business Roundtable and the National Association of Corporate Directors claims that a director who may meet the NYSE's criteria may still not be independent.¹²⁵ They insist that it is necessary to ensure that independent directors are both 'subjectively and objectively independent'.¹²⁶

Unlike to US practice, the management board of a German listed company is not required to have a majority of independent directors. Instead, the requirement is applied

¹¹⁹ However, the studies on the relationship between outside managers and firm performance are mixed. Some scholars found a positive relationship while others found unclear results. See Barry Baysinger and Henry N Butler, 'Corporate Governance and the Board of Directors: Performance Effects of Changes in Board Composition' (1985) 1(1) *Journal of Law, Economics, & Organization* 101; Michael H Schellenger, David Wood and Ahmad Tashakori, 'Board of Director Composition, Shareholder Wealth, and Dividend Policy' (1989) 15(3) *Journal of Management* 457; Scott W Barnhart, M Wayne Marr and Stuart Rosenstein, 'Firm Performance and Board Composition: Some New Evidence' (1994) 15(4) *Managerial and Decision Economics* 329; *ibid.*

¹²⁰ NYSE's Listed Company Manual s 303A.01.

¹²¹ *Ibid* s 303A.02.

¹²² *Ibid* s 303A.02(a).

¹²³ *Ibid* s 303A.02(b).

¹²⁴ *Ibid.*

¹²⁵ Bauman, Weiss, and Palmiter, above n 29, 587.

¹²⁶ *Ibid.*

to the supervisory board.¹²⁷ It, as noted, elects the board of directors. The purpose of the rule is to ensure that the supervisory board is impartial in both its advice and in supervising the management board. The number of independent supervisors is not specified. The rule merely requires “an adequate number” of independent board members.¹²⁸ A supervisory board member is considered independent if there is no business or personal relationships with the company or its management board that produces a conflict of interest.¹²⁹ Du Plessis explained that the German Code did not have a comprehensive definition of independence because there were employee representatives and representatives for the bank serving on the supervisory board and this practice became a part of the German corporate governance system.¹³⁰ Only two former members of the management board are allowed to be members of the supervisory board at any time.¹³¹ Former members of the management board cannot be members of the supervisory boards within two years from the end of their appointment unless they are appointed by motions from shareholders holding more than 25 per cent of the company’s voting rights.¹³² Supervisory board members must not hold positions with or perform advisory tasks for important competitors of the company.¹³³

For Thai listed companies, independent directors must form at least one-third of the board of listed companies and consist of at least three persons.¹³⁴ The rule made by the Thai SEC requires that independent directors and persons to whom they are connected must not hold more than one per cent of the shares in a company or its associated companies.¹³⁵ This was reduced in 2007 from five per cent.¹³⁶ Those who have current financial or managerial interests in the listed company or its associated companies, or during the previous two years, are prohibited from being independent directors.¹³⁷ The

¹²⁷ German Code of Corporate Governance s 5.4.2.

¹²⁸ The research finds that the limitation to “an adequate number” of independent board members is justified. See Lieder, above n 109, 133–4.

¹²⁹ German Code of Corporate Governance s 5.4.2.

¹³⁰ Jean J Du Plessis, ‘The German Two-Tier Board and the German Corporate Governance Code’ (2004) 15 *European Business Law Review* 1139, 1151.

¹³¹ German Code of Corporate Governance s 5.4.2.

¹³² *Ibid* s 5.4.4.

¹³³ *Ibid*.

¹³⁴ SEC Notification No TorJor 4/2552.

¹³⁵ *Ibid*.

¹³⁶ SEC News No 101/2007.

¹³⁷ SEC Notification No TorJor 4/2552.

financial and managerial prohibited relationships include executive directors, employees, and professional advisors, such as auditors, lawyers, and financial advisors.¹³⁸ The controlling shareholders and their family members are also prohibited.¹³⁹ These requirements were introduced in 2007 and were planned to take effect at shareholders' meetings in 2009.¹⁴⁰ However, because of complaints by listed companies of the burden of this higher standard and the global financial crisis, in 2009 the Thai SEC postponed its application to 2010.¹⁴¹

During the course of the interviews conducted for this thesis, the interviewees were questioned on the roles of independent directors. A corporate lawyer explained the connection between independent directors and controlling shareholders and the roles of independent directors:

Practically speaking, it is common that large shareholders will choose members of audit committee and independent directors from those they know. This is because, firstly, it is impossible to choose perfect strangers, and selecting someone who cannot get along with the large shareholders will result in problems of company operation. This consequently affects all parties including minority shareholders. It is argued that some independent directors act like rubber stamps but I disagree. From my experience, independent directors are well aware of their duties. They also perform their duties very well.¹⁴²

An independent director also observed:

Concerning independent directors, in general, they are good but the problem is how good they are. In some cases, independent directors are closely related to the management especially in family owned companies. Insiders, the management, do not want to have many outsiders involved. It is therefore questionable whether and how independent directors can perform their duties independently.¹⁴³

¹³⁸ Ibid.

¹³⁹ Ibid.

¹⁴⁰ SEC News No 101/2007.

¹⁴¹ SEC Notification No KorLorTor.Kor.(Vor) 8/2552.

¹⁴² Interviews with corporate lawyers, Bangkok.

¹⁴³ Interview with a professional independent director, Bangkok.

Nikomborirak has argued that outside directors are well supported by the public and their presence could improve a company's image.¹⁴⁴ However, their decisions may not be good ones. He explained that the amount of time and business skills they contributed to the company were limited.¹⁴⁵

In both the US and Thailand, the regulators attempt to distinguish insiders and outsiders by defining the term "independent".¹⁴⁶ German law, on the other hand, briefly specifies the qualifications of independent directors.¹⁴⁷ In theory, having outsiders on the board can lead to effective monitoring of managers and balancing the power of controlling shareholders. However, it is questionable in Thai culture, where the relationships between people in the same community are very strong, whether it is possible for sufficient numbers of truly independent outsiders to be found. As well, given the character of Thai companies, similar to other Asian companies, the lack of trust in outsiders makes it difficult for unrelated people to be part of a family group.¹⁴⁸ The delayed enforcement of the revised rules also reveals the strength of the Thai business and corporate elite in resisting firmer regulation. Therefore, the purpose of having independent directors limit the representation of a substantial shareholder might not be achieved.

In summary in respect of shareholders' rights to participate in appointing board members, minority shareholders do not have sufficient voting power to elect their preferred candidates. This is because in practice, listed companies do not employ cumulative voting procedures. Under straight voting, majority shareholders always out vote the minority. However, the law in the three jurisdictions ensures that listed companies establish nomination committees to choose well-qualified candidates. In addition the board members must contain a certain number of independent directors. The findings show that, in Thailand, although the requirements of the nomination

¹⁴⁴ Deunden Nikomborirak, 'An Assessment of the Role of Board of Directors in Building Good Governance: The Case of Thailand' (2001) 16(3) *TDRI Quarterly Review* 14, 16.

¹⁴⁵ *Ibid.*

¹⁴⁶ See NYSE's Listed Company Manual s 303A.02; SEC Notification No TorJor 4/2552.

¹⁴⁷ See German Code of Corporate Governance s 5.4.2.

¹⁴⁸ See Francis Fukuyama, *Trust: The Social Virtues and the Creation of Prosperity* (1995). Fukuyama's core thesis is that trust is what makes economic prosperity. He also argued that trust, based on its varied levels, shaped the diverse forms of business organisations.

committee and independent directors are in place, the unsolved issue is how to ensure the independence of the members of both the nomination committee and of independent directors.

4.3 Proprietary rights of shareholders

The previous sections discussed shareholders' management rights in two aspects – the right to participate in management and the right to appoint board members. In addition, shareholders as owners are entitled to a return on their investment. While holding shares, they have the right to participate in earnings and the future growth of the company. They are also free to sell their shares. In this section, the research considers how the law in the three jurisdictions protects the shareholders from dilution of their shares and ensures their entitlement to dividends. The issue of the right to dispose of shares is not considered as minority shareholders in listed companies can always sell shares in the market.

4.3.1 Maintaining the shareholding

The degree of control over a corporation depends on the percentage of the corporation's stock held by each of the shareholders. Some shareholders may be concerned about the dilution of their voting power if additional shares are issued to outsiders or to other existing shareholders. Issuing additional shares may have two effects – equity and economic dilution. Dilution of equity occurs when the percentage of shares held by a shareholder decreases because the proportional voting rights of such a shareholder are reduced.¹⁴⁹ An economic dilution refers to 'the possibility that sales of additional shares will reduce the value of the shares [such shareholder] holds'.¹⁵⁰ To protect the interests of existing shareholders in maintaining their shareholdings in the company, shareholders have a right to accept or not accept additional shares issued by the corporation. This right is known as a "preemptive right".

¹⁴⁹ Bauman, Elliott, and Palmiter, above n 29, 259.

¹⁵⁰ Ibid.

In the US, the concept of a preemptive right was developed by the judiciary as a property right of shareholders.¹⁵¹ In closely held corporations, this right is essential as shareholders often take part in managing the business and want to preserve their voting powers.¹⁵² In publicly held corporations, the preemptive right causes major problems.¹⁵³ It is a burden for companies with multiple classes of shares and a large number of shareholders to organise new share issues to all shareholders. The preemptive right also results in higher costs in fund raising than in issuing new shares on the stock market. In addition, it is questionable whether minority shareholders in large corporations are concerned about their proportionate interests as most public shareholders are passive.¹⁵⁴ They are also able to purchase additional shares directly in the market.¹⁵⁵ DGCL adopts an opt-in approach to preemptive rights. Shareholders are able to subscribe to an additional issue of stock only to the extent that the preemptive right is expressly granted to such shareholders in the certificate of incorporation.¹⁵⁶ In general US practice, however, most public companies do not acknowledge preemptive rights.¹⁵⁷

In German companies, shareholders are entitled to subscribe to new shares in proportion to their holdings of the existing share capital.¹⁵⁸ Existing shareholders retain the right for only two weeks after the publication of the share issuance date.¹⁵⁹ There are exceptions to this requirement: (1) if a capital increase does not exceed 10 per cent of the share capital and the issue price is not materially below the stock exchange price;¹⁶⁰ and (2) shareholders constituting three-quarters, or a larger majority as stated in the articles, of the share capital represented at the shareholders' meeting vote to eliminate wholly or partly the preemptive right.¹⁶¹ The board of management is required to justify any proposal for such elimination in a written report.¹⁶² The acquisition of new shares by a credit institution or similar business organisation is not considered as an exclusion

¹⁵¹ Paul M Coltoff et al, *Corpus Juris Secundum* (2009) § 115.

¹⁵² William M Fletcher, *Fletcher Cyclopedia of the Law of Corporations* (2009) § 5135.

¹⁵³ *Ibid.*

¹⁵⁴ *Ibid*; Bauman, Elliott, and Palmiter, above n 29, 260.

¹⁵⁵ Fletcher, above n 152.

¹⁵⁶ Delaware General Corporation Law § 102(b)(3).

¹⁵⁷ Bauman, Elliott, and Palmiter, above n 29, 260.

¹⁵⁸ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) §§ 186(1), 187(1).

¹⁵⁹ *Ibid* § 186(1).

¹⁶⁰ *Ibid* § 186(3).

¹⁶¹ *Ibid* § 186(3).

¹⁶² *Ibid* § 186(4).

of preemptive rights.¹⁶³ Any offer made before the resolution to increase the share capital is invalid.¹⁶⁴

Unlike US and German law, Thai law does not acknowledge that a company has to offer shareholders newly issued shares. It may be offered, wholly or partly, to existing shareholders in proportion to their shares already held, to the public, or to any other person.¹⁶⁵ The power to decide this belongs solely to the meeting of shareholders.¹⁶⁶ The absence of a requirement for preemptive rights does not affect minority shareholders. In practice, Thai companies are generally controlled by majority shareholders;¹⁶⁷ if controlling shareholders view the increase of capital as beneficial for them, they will pass a resolution permitting them and all other existing shareholders to acquire the additional shares.

4.3.2 Rights to dividends

According to Berle and Means, in modern US corporations, the benefits that minority shareholders expect in exchange for their investments are an increase in the value of the shares and a return on their investment in the form of dividends.¹⁶⁸ The stock market directly reflects the price of companies' shares, while corporate dividend policy solely relies, as noted, on the discretion of the board of directors unless its certificate of incorporation specifies otherwise.¹⁶⁹ In regard to dividend policy, Jensen mentioned in a widely cited articles:

A central weakness and source of waste in the public corporation is the conflict between shareholders and managers over the payment of free cash flow – that is, cash flow in excess of that required to fund all investment projects with positive net present values when discounted at the relevant cost of capital. For a company to operate efficiently and maximise value, free cash flow must be distributed to shareholders rather than retained.

¹⁶³ Ibid § 186(5).

¹⁶⁴ Ibid § 187(1).

¹⁶⁵ Public Limited Companies Act B.E. 2535 (1992) (Thailand) s 137.

¹⁶⁶ Ibid.

¹⁶⁷ See, eg, Stijn Claessens and Joseph PH Fan, 'Corporate Governance in Asia: A Survey' (2002) 3(2) *International Review of Finance* 71; Stijn Claessens, Simeon Djankov and Larry HP Lang, 'The Separation of Ownership and Control in East Asian Corporations' (2000) 58 *Journal of Financial Economics* 81.

¹⁶⁸ Berle Jr and Means, above n 1.

¹⁶⁹ Delaware General Corporation Law § 170(a).

But this happens infrequently; senior management has few incentives to distribute the funds, and there exist few mechanisms to compel distribution.¹⁷⁰

On the one hand, shareholders may expect the management to distribute the company's excess capital. On the other hand, the management may want to retain such cash flow to increase the company's size.¹⁷¹ Such an expansion reflects the performance of the management and may result in an increase in the board's remuneration.¹⁷² Besides, retaining the profits may be necessary for managerial decision-making as a part of investment strategic planning. In public companies, the decision of the directors whether to pay a dividend is very difficult to successfully challenge.¹⁷³ In *Kamin v American Express Co*, for example, the court held that '[m]ore specifically, the question of whether or not a dividend is to be declared or a distribution of some kind should be made is exclusively a matter of business judgment for the [b]oard of [d]irectors'.¹⁷⁴ The court therefore examined only whether the board acts in bad faith and for a dishonest purpose.¹⁷⁵

Contrary to law and practice in US corporations, in German corporations the shareholders' meeting is entitled to declare the appropriate distributable profits based on the company's annual financial statement.¹⁷⁶ In addition, such a declaration includes the amount to be distributed to shareholders, the amount to be transferred to profit reserves, and any profit to be carried forward.¹⁷⁷

Under Thai company law, both the board of directors and the shareholders' meeting are empowered to distribute dividends. Generally, in an annual meeting, the meeting

¹⁷⁰ Michael Jensen, 'Eclipse of the Public Corporation' (1989) 67(5) *Harvard Business Review* 61, 66.

¹⁷¹ Ibid.

¹⁷² Ibid. Cf, eg, Thomas H Lee and John W Childs, 'The Public Corporation: Viewing the Eclipse' (1989) 67(6) *Harvard Business Review* 184; Ira M Millstein, 'The Public Corporation: Viewing the Eclipse' (1989) 67(6) *Harvard Business Review* 192; Peter Róna, 'The Public Corporation: Viewing the Eclipse' (1989) 67(6) *Harvard Business Review* 197; Murray L Weidenbaum, 'The Public Corporation: Viewing the Eclipse' (1989) 67(6) *Harvard Business Review* 204. For Jensen's response, see Michael Jensen, 'The Evidence Speaks Loud and Clear' (1989) 67(6) *Harvard Business Review* 186.

¹⁷³ Pinto and Branson, above n 28, 77.

¹⁷⁴ *Kamin v American Express Co* 383 S 2d 807 (NY, 1976) at 812.

¹⁷⁵ Ibid.

¹⁷⁶ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 119(2).

¹⁷⁷ Ibid § 174(2).

resolves the amount of dividends to be distributed to all members.¹⁷⁸ If the articles of association of the company permit, the board of directors may pay interim dividends to the shareholders when they believe that the company has made sufficient profit to do so.¹⁷⁹ The board is also required to inform the shareholders of the dividend payment at the next shareholders' meeting.¹⁸⁰

The law in the three jurisdictions provides the protection for shareholders to maintain their proportionate interest and the return on their investment in different ways. For US corporations, shareholders have no rights to first acquire additional issued shares and participate in the dividend policy unless the certificate of incorporation specifies otherwise. In Germany on the contrary the power to decide on preemptive rights and the dividend policy are preserved for the shareholders' meeting. Thai law acknowledges the powers of both the board of directors and the shareholders' meeting. Although minority shareholders are not able to dominate the board or the shareholders' meeting, their right to first acquire additional shares or dividends is not affected as the controlling shareholders will pass a resolution protecting their own interests and consequently benefiting all other existing shareholders.

4.4 Conclusion

This chapter considers the rights of minority shareholders under US, German and Thai law from two aspects: their management rights and their proprietary rights. Thai law provides sufficient rights to minority shareholders regarding the right to participate in the meetings, to appoint board members, and to protect their investment. Generally the rules protecting shareholders' rights in the three jurisdictions are similar. The research also questions whether some of the rules adopted by the Thai legal system can practically protect minority shareholders in Thai companies. The mechanisms developed in the US have been based on the agency theory to ensure that the management will act in the interests of the principals, the shareholders, rather than in its own. On the other hand, the conflicts of interests within Thai companies come from

¹⁷⁸ Public Limited Companies Act B.E. 2535 (1992) (Thailand) s 115 paragraph 2.

¹⁷⁹ Ibid s 115 paragraph 3.

¹⁸⁰ Ibid.

concentrated ownership and are between controlling and minority shareholders. Consequently, some of the adopted rules, such as shareholders' proposal and proxy solicitations, do not function in the Thai context. A detailed discussion on the success and failure of transplants is in Chapter 8. As the significant organs of any company comprise the shareholders' meetings and the board of directors, the next chapter will consider the laws and legal practices regarding the board of directors in the US, Germany, and Thailand.

Chapter 5

Duties of Directors and Controlling Shareholders

- 5.1 Introduction
- 5.2 Duties of directors
 - 5.2.1 The general concept of directors' duties
 - 5.2.2 The duty of care
 - 5.2.2.1 Business judgment rule
 - 5.2.3 Duty of loyalty
 - 5.2.4 Avoidance of liability
- 5.3 Fiduciary duties of controlling shareholders
- 5.4 Conclusion

5.1 Introduction

The previous chapter compared of the fundamental rights of minority shareholders in three jurisdictions – the US, Germany, and Thailand. This chapter considers the laws and practices relating to the powers and duties of the board of directors in these jurisdictions. An outline of the scope of directors' duties indicates how the law seeks to deter directors from engaging in misconduct. This is extended to the liability of controlling shareholders. Although controlling shareholders are not empowered to manage a company, they hold sufficient voting powers to appoint members of the management board and to determine a company's direction. In some situations they may act as *de facto* or shadow directors.

5.2 Duties of directors

5.2.1 The general concept of directors' duties

In company law, the area that draws significant attention in the US literature is the delegation of power over the company's management. Power is passed from the residual owners, the shareholders, to the management to perform some actions on the shareholders' behalf. As mentioned in Chapter 2, Jensen and Meckling argued that the

delegation of power to management created agency problems.¹ The risk exists that the agents may not act in the interests of the principals. The principals expect the agents to maximise their profits but the agents may be concerned with self-interest and put their own interests over those of the principals. A central issue is the role of law in controlling or minimising this agency problem. As indicated in Chapter 2, conflicts of interests and agency problems are different in German and East Asian listed companies.

Common law jurisdictions consider a director to be a fiduciary.² The word *fiduciary* comes from the Latin *fides*, meaning faith or confidence. The fiduciary agrees to act on behalf and in the interests of another person. The decision made by the fiduciary affects the interests of that other person.³ The fiduciary has a duty to use the given power to benefit that other person. The fiduciary institution is applied to a variety of relationships, such as trustee and beneficiary; agent and principal; solicitor and client; executor and heir; and, director and company.⁴ The responsibilities imposed on the fiduciary vary depending on the context. They are highest in the relationship between trustee and beneficiary. The relationship between the company and a director is at a lower level. The directors are expected to take commercial risks in order to generate profit for the company. In practice, and in law, judges tend to defer to directors' decision if the directors have no personal interests in the transaction. This is known as the "business judgment rule" which will be discussed later in this chapter. Civil law jurisdictions also acknowledge the concept of faith or confidence. Section 5 of the Thai Civil and Commercial Code, for example, requires that every person must, in the exercise of a right and in the performance of an obligation, act in good faith. In Thai, this is *sujarid* which has been derived from the Roman concept of *bona fides* and which can be literally translated as *honesty or integrity*. This provision applies to any

¹ The agency problem is discussed in Chapter 2.

² For a discussion on the fiduciary duties of directors, see Walter R Hinnant, 'Fiduciary Duties of Directors: How Far do They Go?' (1988) 23 *Wake Forest Law Review* 163; Roger Edgar, 'Corporations: The Fiduciary Duty, a Trend in the Law' (1962–1963) 7 *St Louis University Law Review* 143; Cleveland Miller, 'The Fiduciary Duties of a Corporate Director' (1974–1975) 4 *Baltimore Law Review* 259; Holly M Barbera, 'Fiduciary Duties and Disclosure Obligations: Resolving Questions after *Malone v Brincat*' (2001) 26(2) *Delaware Journal of Corporate Law* 563; Gregory Scott Crespi, 'Rethinking Corporate Fiduciary Duties: The Inefficiency of the Shareholder Primacy Norm' (2002) 55(1) *SMU Law Review* 141; John F Mariani, Christopher W Kammerer and Nancy Guffey-Landers, 'Understanding Fiduciary Duty' (2010) March(84) *Florida Bar Journal* 20.

³ *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 96.

⁴ Mariani et al, above n 2, 20.

contractual relationship. Its scope and context varies with the context. Thai company law employs the standard of a careful businessperson.⁵ Despite its origin in a different legal system, it is widely accepted that directors are fiduciaries for the company in Thai law.

Yet there are contrary views to this general acceptance. One of the most contentious issues regarding directors' duties is to what extent a court should scrutinise the decisions made by them.⁶ The literature generally recognises that there is a divergence between the interests of directors and shareholders, and that the shareholders are unable to control the directors.⁷ Potentially, strong protection for shareholders from powerful management may be required.⁸ This suggests that the law should establish high standards to prevent fraud and corporate dysfunctionality.⁹ However, scholars from a law and economics perspective propose a contrary approach. In the "nexus of contracts" model, the corporation becomes a series of agreements among participants.¹⁰ The relationship between directors and shareholders, as well as those among shareholders themselves, are found by the terms of these contracts. The parties' rights and obligations, including the fiduciary duties of directors, are considered only as terms of a contract.¹¹ This contractarian theory views corporate law as having the same functionality as contract law, a transaction facilitator. As negotiating each contract would be time-consuming and costly, the law institutes a set of default rules so that

⁵ The specific details on the standard of care are discussed later in this chapter.

⁶ Honorable Veasey, the former Chief Justice of Delaware, pointed out:

Stockholders vote for directors and expect proper governance from them. The expectation is a strong board of trust vested in the directors. Courts enforce that trust. At the same time, courts should be reluctant to interfere and should not create surprises or wild doctrinal swings in their expectations of directorial [behaviour].

E Norman Veasey, 'The Stockholder Franchise Is Not a Myth: A Response to Professor Bebchuk' (2007) 93(3) *Virginia Law Review* 811, 13.

⁷ See, eg, Adolf A Berle Jr and Gardiner C Means, *The Modern Corporation and Private Property* (1933); Eugene F Fama and Michael Jensen, 'Agency Problems and Residual Claims' (1983) 26 *Journal of Law and Economics* 327.

⁸ Julian Velasco, 'The Fundamental Rights of the Shareholder' (2006) 40 *UC Davis Law Review* 407, Part III.

⁹ Joel Seligman, 'The New Corporate Law' (1993) 59(1) *Brooklyn Law Review* 1; Dennis J Block, Michael J Maimone and Steven B Ross, 'Duty of Loyalty and the Evolution of the Scope of Judicial Review' (1993) 59(1) *Brooklyn Law Review* 65; William T Quillen, 'Federal-State Corporate Law Relationship – A Response to Professor Seligman's Call for Federal Preemption of State Corporate Fiduciary Law' (1993) 59(1) *Brooklyn Law Review* 107.

¹⁰ Henry N Butler, 'The Contractual Theory of the Corporation' (1989) 11(4) *George Mason University Law Review* 99, 99–100.

¹¹ Arthur R Pinto and Douglas M Branson, *Understanding Corporate Law* (2nd ed, 2004) 204.

parties are efficiently able to enter into a contract.¹² The parties to contracts in this nexus may adjust the default rules. The power of the courts should be limited to the enforcement of the terms of any contracts.¹³ This view may be problematic as the relationship between directors and the company is distinctive and fiduciary duties are different from duties in contract law.

Given the different origins and approaches to the directors' duties, this section, through statutes and judicial interpretation and decisions, focuses on how directors' duties in the three jurisdictions have been developed and how they are currently defined. It begins with the duty of care – the duty to perform the duties to an appropriate standard – then discusses the duty of loyalty – the duty to act in the best interests of the company and in good faith.

5.2.2 The duty of care

The law in all three jurisdictions addresses the issue that directors may act carelessly. This aspect of agency in the management of shareholders' capital was observed by Adam Smith. As he rightly pointed out, directors are the managers of other people's money rather than of their own.¹⁴ It cannot be expected that they will watch over it with the same anxious vigilance.¹⁵ How the law in the three jurisdictions ensures that the directors will act with care and competence is outlined referring to both legislation and case law. The business judgment rule in the three jurisdictions is described to show it protects directors to varying degrees when the decision they make is on an informed basis and in good faith.

¹² Frank H Easterbrook and Daniel R Fischel, 'The Corporate Contract' (1989) 89 *Columbia Law Review* 1416, 1444. See also Lewis A Kornhauser, 'Nexus of Contracts Approach to Corporations: A Comment on Easterbrook and Fischel' (1989) 89 *Columbia Law Review* 1449.

¹³ Butler, above n 10, 100.

¹⁴ Adam Smith, *Wealth of Nations* (1776) 700.

¹⁵ *Ibid.*

United States

There is no codification of the duty of care in the Delaware General Corporation Law. The Model Business Corporation Act (“MBCA”) restates common and legislative law in the US. Under it, directors must ensure that they take all relevant information into consideration and perform their duties ‘with the care that a person in a like position would reasonably believe appropriate under similar circumstances’.¹⁶ As initially adopted in the 1984 version of the MBCA, the standard was ‘the care [that] an ordinarily prudent person in a like position would exercise under similar circumstances’. It was amended to the present ‘the care that a person in a like position ...’.¹⁷ The ‘ordinary prudent person’ previously used in the MBCA is a standard mainly found in tort law to recognise the difference between the standards applied to people in general and to people exercising specialised skills.¹⁸

These principles and the contexts, in which they apply, are established in the case law. In *Francis v United Jersey Bank*,¹⁹ the New Jersey Supreme Court set out the general responsibilities of directors. The court held that the ordinary care which the directors should observe includes: (i) understanding the business of the corporation,²⁰ (ii) keeping informed about its activities,²¹ (iii) monitoring corporate affairs and policies,²² (iv) maintaining familiarity with its financial status by a regular review of financial statements,²³ and (v) seeking advice from experts.²⁴ The court also recognised the higher responsibility of directors in large, publicly held corporations.²⁵ It stated that ‘[a] director is not an ornament, but an essential component of corporate governance.

¹⁶ The Model Business Corporation Act (2002) § 8.30(a). For a discussion on the development of the duty of care under the MBCA, see Tamar Frankel, ‘Corporate Directors’ Duty of Care: The American Law Institute’s Project on Corporate Governance’ (1983–1984) 52 *George Washington Law Review* 705.

¹⁷ The Model Business Corporation Act § 8.30(a) (1984).

¹⁸ The Model Business Corporation Act § 8.30 Official Comment.

¹⁹ *Francis v United Jersey Bank* 432 A.2d 814 (NJ, 1981).

²⁰ *Ibid* 821–2.

²¹ *Ibid* 822.

²² *Ibid*.

²³ *Ibid*.

²⁴ *Ibid*.

²⁵ *Ibid* 824.

Consequently, a director cannot protect himself behind a paper shield bearing the motto, “dummy director””.²⁶

In respect of the duty of monitoring corporate affairs and policies, the Delaware Supreme Court first created the director’s duty to monitor for legal compliance in 1963. In *Graham v Allis-Chalmers Mfg Co*,²⁷ a derivative action was brought against the directors and four non-director employees of Allis-Chalmers. The company and those employees had been indicted for violations of federal anti-trust laws. The shareholder plaintiffs claimed that the directors had failed to take action to institute a monitoring system to prevent anti-trust violations. The court held that, although the directors had no knowledge of any suspicion of wrongdoing by the employees, the directors should have put into effect a system of watchfulness.²⁸ However, it stated that the directors were also entitled to rely on the honesty and integrity of the employees until something occurred to make them suspicious.²⁹ In this case, as there was no cause to suspect anti-trust violations, the directors had no duty to install a monitoring system. One may argue that the decision is justified as Allis-Chalmers employed in excess of 30,000 people and the company’s directors could not know all the employees.³⁰ It could also be argued that the court affirmed a weak standard that, with the absence of suspicion of the deception, a corporate board can discharge its duty simply by relying on the integrity and honesty of employees.³¹

In 1996, the Delaware court in *In re Caremark Intern Inc Derivative Litigation*³² raised the standard required for oversight by overturning the standard established in *Graham*. *Caremark* had to pay US\$250 million in fines and damages caused by its employees violating health care regulations. The shareholders brought a derivative suit against the company’s board alleging that the board breached its duty as it failed to monitor the employees. The court found that recent business trends required directors to be more

²⁶ Ibid.

²⁷ *Graham v Allis-Chalmers Mfg Co* 188 A.2d 125 (Del Ch, 1963).

²⁸ Ibid 130.

²⁹ Ibid.

³⁰ Ibid.

³¹ Jeffrey T Dinwoodie, "Unpatriotic" Profits: The Risks Companies Face from International Business Activities and the Need for a Heightened Duty of Oversight for Corporate Directors' (2009) 34 *University of Dayton Law Review* 377, 386.

³² *In re Caremark Intern Inc Derivative Litigation* 698 A.2d 959 (Del Ch, 1996).

attentive. The board had an obligation to monitor the corporation's activities and to assure itself that there were monitoring systems in place to provide it with timely and accurate information on the corporation's compliance with the law.³³

Germany

German law has taken a different approach to directors' duties to that of US law. Baums explained that the difference to be found between the principles of agency and trust law and the concept of directors as "organs".³⁴ Common law applied the concept of agency and trust law to develop the directors' duties. German law developed from the recognition of the management and supervisory boards as the "organs" of a company. This legal concept 'shows a tendency to ascribe these organs an autonomous position and independent competences, and seems less suitable to underline their serving [sic]'.³⁵ Vitols further explained that, unlike the strong CEO model in US companies, both management and supervisory boards in German companies support a consensus approach to decision making. They make an effort to find a unanimous decision rather than one obtained by a majority vote.³⁶

Unlike in Delaware law, the duty of care in German law is mainly codified. Article 93 of the *Aktiengesetz* of 2009 [Stock Corporation Act] ("*AktG*") requires that, in conducting business, the members of the management board employ the care of a diligent and conscientious manager. A broad standard is applied to allow adequate judicial discretion in evaluating the performance of the members of the management board.³⁷ The standard of care of a diligent and conscientious manager imposed in

³³ Ibid 970. In responding to *Graham*, the court stated that:

[A]bsent grounds to suspect deception, neither corporate boards nor senior officers can be charged with wrongdoing simply for assuming the integrity of employees and the honesty of their dealings on the company's behalf.

Ibid 969.

³⁴ Theodor Baums, 'Personal Liabilities of Company Directors in German Law' (Speech delivered at the Stratford-upon-Avon Conference of the British-German Jurists' Association, 21 April 1996) 7–8.

³⁵ Ibid 8.

³⁶ Sigurt Vitols, 'German Corporate Governance in Transition: Implications of Bank Exit from Monitoring and Control' (2005) 2(4) *International Journal of Disclosure and Governance* 357, 360–1.

³⁷ Willi Joachim, 'The Liability of Supervisory Board Directors in Germany' (1991) 25 *The International Lawyer* 41, 59–60.

Article 93 is applied to both the members of the management board and the supervisory boards.³⁸

In addition to the general standard, the *AktG* imposes specific duties on members of both the management and supervisory boards. The management board is required to establish a monitoring system for the early detection of any changes exposing the company to severe risk.³⁹ If the company has incurred a loss equal to one-half of its share capital, the management board must promptly call a shareholders' meeting to inform the shareholders of the loss.⁴⁰ This duty requires the board to continually review the financial statements of the company. For the members of the supervisory board, the law requires them to: (i) attend the meetings of the supervisory board which are held, for listed companies, four times a year;⁴¹ (ii) inspect and examine the books and records of the company;⁴² and, (iii) call a shareholders' meeting whenever the interests of the company require it.⁴³ The management board has an obligation to promptly submit the annual financial statements and reports to the supervisory board on their completion.⁴⁴ After examining such statements and reports, the supervisory board has to report the result of their examination to the shareholders' meeting.⁴⁵ As the supervisory board consists of the representatives from both shareholders and labour, it is questionable whether similar standards are equally applicable to both. One may argue that generally shareholders' representatives are elected from those who have considerable business skills, such as bankers, executives from major business partners, lawyers or other professionals.⁴⁶ However, despite the fact that the labour representatives may have comparably lower professional and commercial expertise than the shareholders' representatives,⁴⁷ the standard of care applied to representatives of labour and shareholders is identical.⁴⁸

³⁸ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 116.

³⁹ *Ibid* § 91.

⁴⁰ *Ibid* § 92.

⁴¹ *Ibid* § 110(3).

⁴² *Ibid* § 111(2).

⁴³ *Ibid* § 111(3).

⁴⁴ *Ibid* § 170(1).

⁴⁵ *Ibid* § 171(1)–(2).

⁴⁶ Klaus J Hopt, 'New Ways in Corporate Governance: European Experiments with Labor Representation on Corporate Boards' (1983–1984) 82 *Michigan Law Review* 1338, 1361.

⁴⁷ Joachim, above n 37, 60.

⁴⁸ *Ibid*.

In addition to the duties stated in legislation, the German courts have by interpretation, further defined the scope of the duty of care. The Supreme Court in *Hertie*⁴⁹ also ruled that each director must have certain minimum qualifications to enable them to understand and make decisions about the company's business.⁵⁰ These minimum standards include the ability to comprehend the company's business and financial statements.⁵¹

Thailand

Under Thai law, similarly to German law, the directors' duty of care in listed companies is mainly defined by statute. The duty of care is firstly codified in the Civil and Commercial Code that governs private companies. Section 1168 specifies that the directors must, in their conduct of the business, apply the diligence of a careful businessperson. The Securities and Exchange Act of 1992 ("Securities Act") as amended in 2008 defines it using different concepts but the effect appears to be similar. The directors are required to act in a similar way to an ordinary person undertaking a like business under similar circumstances.⁵² In considering whether directors have exercised due care, the following factors are taken into account: (i) their position in the company; (ii) their scope of responsibility in such positions in accordance with the laws and as assigned by the board; and, (iii) their qualifications, knowledge, capabilities, as well as experience, including the purpose of their appointment.⁵³

These provisions have not been further refined or interpreted by the Supreme Court in respect of a director in a public company. No case has been brought to it.⁵⁴ The few cases in the Supreme Court involving the directors of private limited companies give some indication of how it applies the duty of care. It previously took a narrow view. In

⁴⁹ *Bundesgerichtshof* [German Federal Court of Justice], II ZR 27/82, 15 November 1982 reported in (1982) 85 BGHZ 293.

⁵⁰ Joachim, above n 37, 60–1.

⁵¹ *Ibid* 61.

⁵² Securities and Exchange Act B.E. 2535 (Thailand) s 89/7.

⁵³ *Ibid* s 89/9.

⁵⁴ Information based on the search engine provided by the Supreme Court website as of March 2012 at <http://www.deka2007.supremecourt.or.th/deka/web/search.jsp>.

Boorapa Insurance Co,⁵⁵ the trustee in bankruptcy brought an action against a director for breach of the duty of care. The director claimed he should not be liable because he was only a general director, not a managing director, having no authority to make decisions. The court held that the action of a non managing director should be treated as that of an individual agent of the company and not as a collective action by the board carrying joint liability for all the directors. However, this holding was later overturned. In *Siam Bank*⁵⁶ and *Vimon*,⁵⁷ the Supreme Court affirmed that the fact that directors who were not familiar with the company's business, were not working as full-time directors, or who hardly visited the company's office had no defence against a claim of breaching the duty of care. Each director was required to oversee the whole of the company's business, although the responsibilities of each director might be different. Directors must have a sufficient understanding of the company's business.⁵⁸

The scope of due care is still significantly limited. In *Banyad*⁵⁹ the company was sued by the plaintiff for damages in a gas explosion caused by one of its employees. The plaintiff alleged that the directors should be jointly responsible for such damages as the company had not obtained the permits required for transporting gas and had allowed the employee to use a truck without a system for preventing explosions. Under Section 1169 of the Civil and Commercial Code, the company, or the company's creditor, can make a claim against directors for compensation for injury caused by them. The court held that the plaintiff was damaged by acts of the company's employee, not the directors, who were not liable to the plaintiff. The court affirmed that using a truck with no systems in place for preventing gas explosions was improper and had had severe consequences. However, the accident was not the direct result of using the truck. As the directors were not liable to the company, they were not jointly liable to the company's creditors. Five years later, a similar case, *Sangpedpanich*,⁶⁰ was heard. The court again found in favour of the directors. In both cases the court narrowly limited the scope of the duty of care. The criterion which the court applied was whether the directors directly

⁵⁵ Decision of the Supreme Court No 1980/2519 (*Boorapa Insurance Co* case).

⁵⁶ Decision of the Supreme Court No 2191/2541 (*Siam Bank* case).

⁵⁷ Decision of the Supreme Court No 977/2545 (*Vimon* Case).

⁵⁸ See *Siam Bank* and *Vimon* cases.

⁵⁹ Decision of the Supreme Court No 4546/2540 (*Bunyad* case).

⁶⁰ Decision of the Supreme Court No 3771/2545 (*Sangpedpanich* case).

caused the damage. If the damage was not the direct consequence of the directors' decision, they were not liable. However, it may be argued that, although the directors did not directly cause the explosion, as the directors of a high-risk business, they had a duty to ensure that both risky and potential damage was minimised and that a system was in place to ensure it drawn to their attention if this was not done. Without doing so, it is questionable whether the directors had properly fulfilled their duty.

5.2.2.1 Business judgment rule

The business judgment rule was originally developed in the practice of common law judges and more recently been restated in legislation. It appears, at first glance, to be inconsistent with the high standards set for board of directors which are 'charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of its shareholders'.⁶¹ Yet the business judgment rule is considered to be a basic principle.⁶² The rule precludes a court from imposing its opinions and decisions arbitrarily on the company's business and affairs.⁶³ As mentioned, unlike beneficiaries in trust, shareholders in companies are more conscious of risk-taking by the management to make a profit. It also recognises the dangers of the use of hindsight.

Although the business judgment rule potentially immunises individual directors against liability to shareholders, there are rationales for limiting the judicial review of business decisions. Firstly, without this rule, litigations brought against directors' decisions potentially turns a court into a "super boardroom", reassessing every minor business decision.⁶⁴ A filter is required to screen out unmeritorious cases. Secondly, due to lack of experience, knowledge, and business skills, judges are not in a position to evaluate those decisions.⁶⁵ They are not equipped to make commercial decisions. Thirdly, there is an alternative means for shareholders to protect their interests – selling their shares in

⁶¹ *Cede & Co v Technicolor Inc* 634 A.2d 345 (Del, 1993) 360.

⁶² *Ibid.*

⁶³ *Ibid.*

⁶⁴ Johneth C Park and Doo-Ah Lee, 'The Business Judgement Rule: A Missing Piece in the Developing Puzzle of Korean Corporate Governance Reform' (2003) 3(2) *Journal of Korean Law Review* 15, 30.

⁶⁵ *Ibid.*

the market.⁶⁶ The market mechanism only gives some redress to each shareholder, but it also helps to control directors' behaviour.⁶⁷ If a large number of shareholders sell a company's shares, this may be a signal to outsiders to take over the company and the board of directors may be replaced. In an efficient and liquid market, the economic remedy may be a better result than the judicial one.⁶⁸ Fourthly, the rule ensures that the directors are in charge of managing the company, not the shareholders or the courts, and it encourages the directors to take appropriate business risks.⁶⁹ These rationales support the underlying principle of corporate law which vests decision-making power in a board of directors elected by the shareholders. The shareholders, in exchange, obtain a share in an enterprise's profits. To make a profit, the board of directors must take some risks.⁷⁰ Shareholders must therefore assume the risks that may occur from bad judgments.⁷¹ In the absence of a business judgment rule, the directors will be reluctant to take any business opportunity and will be concerned with only their personal liability.⁷² Last of all, the business judgment rule encourages outsiders with skills and integrity to serve on the board as the law does not impose an excessive degree of care on them.⁷³

The Supreme Court of Delaware described the business judgement rule as:

[A] presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. ... Absent an abuse of discretion, that judgment will be respected by the courts. The burden is on the party challenging the decision to establish facts rebutting the presumption.⁷⁴

⁶⁶ Ralph S Peeples, 'The Use and Misuse of the Business Judgment Rule in the Close Corporation' (1984–1985) 60 *Notre Dame Law Review* 456, 461.

⁶⁷ *Ibid* 461–2.

⁶⁸ *Ibid* 461.

⁶⁹ See Delaware General Corporation Law § 141(a).

⁷⁰ Alfred D Mathewson, 'Decision Integrity and the Business Judgment Rule: A Theory' (1989–1990) 17 *Pepperdine Law Review* 879, 879.

⁷¹ *Ibid*.

⁷² Franklin Balotti and James J Jr Hanks, 'Rejudging the Business Judgment Rule' (1992–1993) 48 *Business Lawyer* 1337, 1341–2; William M Fletcher, *Fletcher Cyclopaedia of the Law of Corporations* (2009) § 1037.

⁷³ Samuel Arsht, 'The Business Judgment Rule Revisited' (1979–1980) 8 *Hofstra Law Review* 93, 97; Douglas M Branson, 'The Indiana Supreme Court Lecture: The Rule that Isn't a Rule – the Business Judgment Rule' (2001–2002) 36 *Valparaiso University Law Review* 631, 637.

⁷⁴ *Aronson v Lewis* 473 A.2d 805 (Del, 1984) 812.

The business judgment rule not only establishes a presumption in favour of the validity of directors' decisions, but it also establishes a procedural rule. To rebut such a presumption, a plaintiff has the burden of proving that directors breached their duty of loyalty.⁷⁵ If the plaintiff fails to do so, the business judgment rule protects the directors and their decisions.⁷⁶ The court will also not second-guess the directors' business judgments.⁷⁷ If the plaintiff can rebut the business judgment rule, the burden will shift to the directors to prove that any challenged transactions are fair to the corporation.⁷⁸ The business judgment rule may not protect the directors if they are negligent in making poorly informed decisions. In *Smith v Van Gorkom*,⁷⁹ the board of directors voted to sell the company in a cash-out merger proposal without sufficient information and under the influence of its chair. Although the directors claimed that there was a substantial premium in the sale price (US\$55 compared with the market price of US\$38), the court held that the board failed to ascertain the real value of the company but accepted the price represented by the chair. Also the board's decision was made after only two hours' consideration, without any considered advice on the proposal or an alternative to it or a reason to act swiftly. The suggested level of carelessness resulted in the business judgment rule providing no protection to the directors.

In Germany, the concept of the business judgment rule is also acknowledged. Baums pointed out its existence in German company law and how the court had crystallised it. He stated that 'the standard of a "prudent business man" says more about how a director has to act rather than what he has to do or should have done'.⁸⁰ This implies judicial self-restraint. The Federal Court of Justice acknowledged the business judgment rule in *ARAG v Garmenbeck*.⁸¹ The court affirmed that 'there is a [boundary] between the violation of the duty of care and loyalty, and entrepreneurial faults in the conduct of the

⁷⁵ *Cede & Co v Technicolor Inc* 634 A.2d 345 (Del, 1993) 361.

⁷⁶ *Ibid.*

⁷⁷ *Ibid.*

⁷⁸ *Ibid.*

⁷⁹ *Smith v Van Gorkom* 488 A.2d 858 (Del, 1985).

⁸⁰ Baums, above n 34, 9.

⁸¹ *Bundesgerichtshof* [German Federal Court of Justice], II ZR 175/95, 21 April 1997 reported in (1997) 135 BGHZ 244.

company'.⁸² Similarly to Delaware court approach, the German court recognised the need to give a management board member the 'wide range of free discretion'.⁸³ A management board member was liable:

[O]nly when [the] manager goes significantly beyond the limits of a business judgment [characterised] by responsible management oriented solely towards the good of the corporation and based on a careful evaluation of the relevant facts.⁸⁴

The decision affirms the existence of such a rule in German corporate law⁸⁵ and some writers suggest that the decision is influenced by the common law business judgment rule.⁸⁶

Later in 2005 the business judgment rule was codified in the *AktG* in the *Ge-setz zur Unternehmensintegrität und Modernisierung des Aktiengesetzes* of 2005 [Law on Corporate's Integrity and on the Modernization of the Stock Corporations Act].⁸⁷ This Act makes changes to German company law, including the business judgment rule and derivative actions,⁸⁸ which will be discussed in Chapter 7. Its purpose is both to encourage minority shareholders to sue misbehaving board members and to reduce the liability of board members.⁸⁹ Under Article 93(1) of the *AktG*, the members of the management and supervisory boards are not liable if: (i) they make a business decision based on sufficient information; and, (ii) they have good reasons to believe that they are acting in the best interests of the company. The members of the management and

⁸² York Schnorbus, 'Tracking Stock in Germany: Is German Corporate Law Flexible Enough to Adopt American Financial Innovations' (2001) 22 *University of Pennsylvania Journal of International Economic Law* 541, 613.

⁸³ Andreas Cahn and David C Donald, *Comparative Company Law: Text and Cases on the Laws Governing Corporations in Germany, the UK, and the USA* (2010) 379.

⁸⁴ Ibid. If the supervisory board found that the management board was liable for damages, it had to bring a legal action against the wrongdoers because initiating such a legal action was part of the supervisory board's duty to supervise the management board. Carsten Jungmann, *Responsibility and Liability of the Management Board* (2009) Dusseldorf Law School <[http://www.duslaw.eu/files/Responsibility%20and%20Liability%20of%20the%20Management%20Board%20\(Jungmann\).pdf](http://www.duslaw.eu/files/Responsibility%20and%20Liability%20of%20the%20Management%20Board%20(Jungmann).pdf)> at 20 March 2012, 2.

⁸⁵ Schnorbus, above n 82, 612.

⁸⁶ Tamo Zwinge, 'An Analysis of the Duty of Care in the United Kingdom in Comparison with the German Duty of Care' (2011) 22(2) *International Company and Commercial Law Review* 31, 35.

⁸⁷ Jean J Du Plessis, Bernhard Grobfeld and Claus Luttermann, *German Corporate Governance in International and European Context* (2007) 60; Latham & Watkins Corporate and Litigation Departments, 'The German Act Regarding Integrity of Companies and Modernization of Stock Corporation Law (UMAG)' (Report No 471, Latham & Watkins, 2005).

⁸⁸ Petri Mäntysaari, *Comparative Corporate Governance: Shareholders as a Rule-maker* (2005) 343.

⁸⁹ Ibid.

supervisory boards bear the burden of proof that they have used the care of a diligent and conscientious manager.⁹⁰ The language of the provision is broad. It gives room for German courts to further develop the principle in case law.⁹¹ In practice, German directors and supervisors almost never face a claim that they have breached the duty of care as shareholders and the corporations usually resolve the issue by not re-electing such directors.⁹²

In Thailand, the business judgment rule is relatively new. Neither statute law nor the case law of the Supreme Court had acknowledged this rule until 2008 when the revised Securities Act including such a rule came into effect. Under Section 89/8 of the Securities Act, the directors are not liable for any decision if it is found that the decision is made: (i) with an honest belief and on reasonable grounds that it is in the best interests of the company; (ii) in reliance of information honestly believed to be sufficient; and, (iii) without the directors' having an interest in the decision, whether directly or indirectly.⁹³ During the interviews conducted for this thesis, the researcher questioned the independent directors about the business judgment rule. All of them felt that the business judgment rule was their safe harbour. One independent director further explained:

Even though we are not sheltered by the business judgment rule, we ensure that the decision is made on an informed basis. Research is done to inform the decision of the management. We also seek advice from professional consultants if necessary. The business judgment rule encourages us to make a decision without fear of being sued if the result of the decision is different from what we expected.⁹⁴

In summary, the rules on the duty of care in the three jurisdictions are similar – company directors are required to act with care, and, in a similar manner as a person in the same position. The idea of a legislative business judgment rule has been primarily developed in the US and has recently been adopted in civil law countries, including

⁹⁰ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 93(2).

⁹¹ Schnorbus, above n 82, 612.

⁹² Theodor Baums and Kenneth E Scott, 'Taking Shareholder Protection Seriously? Corporate Governance in the United States and Germany' (2005) 17(4) *Journal of Applied Corporate Finance* 44, 50.

⁹³ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/8.

⁹⁴ Interview with a professional independent director, Bangkok.

Germany and Thailand. Despite these similarities, the paths to this position in these three jurisdictions are significantly different. In the US, the courts play a leading role in determining the legal rules and principles relating to the duty of care and the business judgment rule. Their application of these rules has changed from time to time in accordance with business trends and public expectations. For instance, in *Graham* the court raised the standard of the duty of oversight and affirmed that the board must ensure that monitoring systems are put in place to limit any risk of damage to the company. Furthermore, the consequences of the collapse of large corporations, including Enron and WorldCom, a decade ago, and the recent financial crisis, have raised public expectations about the standard of care. In Germany and Thailand, the range of the duty of care is narrower and less developed than in the US law system. It has been mainly developed by legislation. Given the limited number of cases brought to the courts, the courts in Germany and Thailand have had less opportunity to develop corporate law through judicial interpretation.

In Thailand, before the introduction of the more detailed duty of care and the business judgment rule in 2008, the Thai court had neither clarified the scope of the duty of care⁹⁵ nor recognised the existence of a business judgment rule. It is questionable whether the adopted rules will function effectively in practice. During the course of the interviews, an academic researcher pointed out the difficulties of further defining the scope of the duty of care:

Before the enactment of the revision of the Securities Act, the scope of the directors' duties was defined by the Public Limited Company Act. [Section 85 of t]he Act briefly required that directors must perform their duties with care to maintain the interests of the company. However, the definition of "care" was unclear. How do we define the meaning of "care"? Which standards should be used to limit its scope? How do we judge whether a director has performed his duty with "sufficient care"? The revised Securities Act came into effect in 2008. The scope of the duty of care has not been clearly defined and the idea of business judgment rule is added instead. It is important to keep in mind that it is impossible for legislators to draft a law containing all the

⁹⁵ See Same Varayudej, 'Company Directors' Duties under the Good Corporate Governance Systems and Lessons from the Pin Chakkaphak Case' (2002) 32 *Thammasat Law Journal* 154, 164.

possible directors' duties. The details of the duty must be based on a case-by-case basis and should be shaped by judicial interpretation.⁹⁶

A legal practitioner affirmed this view and explained why the Thai court has had limited opportunity to define the duty of care:

The main reason that the scope of the duty of care is unclear is the limited number of cases brought to the court. As contingent fees are not allowed in Thailand, cases brought against directors are very rare. We adopted the concept of derivative actions but, practically speaking, minority shareholders have no incentive to bring an action as they cannot see any benefit from it. Plaintiff shareholders have to pay for all the fees by themselves, although, later, the court may reimburse the expenses. The procedure in the court is time consuming. Importantly they do not believe that they are going to win the case. There is no precedent on which plaintiff shareholders can rely. The information is all in the hands of the management. It is not surprising why minority shareholders prefer to walk out of the company rather than sue directors who have misbehaved. Consequently the court has no chance to define the scope of the duty of care.⁹⁷

Unlike the US practice in which minority shareholders often bring derivative actions against directors, no case has been brought to the Thai Supreme Court against directors of public companies. In the absence of the enforcement by the court of the duty of care, the new statutory rules may not bring any changes in practice to the Thai legal system.⁹⁸

5.2.3 Duty of loyalty

When a decision of the directors may confer benefit on the directors, the duty of loyalty needs to be considered. It requires the fiduciary, the director, to put the interests of the beneficiary, the company, ahead of his own interests.⁹⁹ Even when fiduciaries have a conflict of interest with the corporation, they have to act or deal fairly.¹⁰⁰ The issue becomes more complex when a self-interested transaction must be approved by

⁹⁶ Interview with an academic researcher, Bangkok.

⁹⁷ Interview with a legal practitioner, Bangkok.

⁹⁸ The detailed discussion on the limited role of the judiciary is in Chapter 7.

⁹⁹ Mariani et al, above n 2, 22.

¹⁰⁰ Melvin Aron Eisenberg, 'The Divergence of Standards of Conduct and Standards of Review in Corporate Law' (1993–1994) 62 *Fordham Law Review* 437, 450.

disinterested directors.¹⁰¹ In such circumstances the definition of “disinterested directors” and of “self-interested transactions”, the approval procedures, and the standard of review for substantive fairness are all-significant.¹⁰² This section describes how the three jurisdictions regulate potential self-dealing by directors.

The US law on directors’ conflict of interest with the company has changed.¹⁰³ In 1880 the law was that ‘the corporation was entitled to the unprejudiced judgment and advice of all its directors and therefore it did no good to say that the interested director did not participate in the making of the contract on behalf of the corporation’.¹⁰⁴ By 1910 the law had changed so that ‘a contract between a director and his corporation was valid if it was approved by a disinterested majority of his fellow directors and was not found to be unfair or fraudulent by the court if challenged’.¹⁰⁵ Finally, by 1960 the present version of the rule had appeared:

No transaction of a corporation with any or all of its directors was automatically voidable at the suit of a shareholder, whether there was a disinterested majority of the board or not; but that the courts would review such a contract and subject it to rigid and careful scrutiny, and would invalidate the contract if it was found to be unfair to the corporation.¹⁰⁶

In Delaware, interested director transactions are governed by Section 144 of the Delaware General Corporation law (“DGCL”). Transactions between a company and one or more directors, or those between a company and other organisations in which one or more directors have a financial interest are valid if: (i) the material facts such as the directors’ interests or relationships are known to the board and the board in good faith authorises such transactions by the affirmative votes of a majority of disinterested directors; (ii) the material facts of the directors’ relationship or interest are known to the shareholders and the shareholders approve such transactions in good faith; or, (iii) the transactions are fair to the corporation as of the time at which they are authorised or

¹⁰¹ Ibid 452.

¹⁰² Ibid 452–3.

¹⁰³ Harold Marsh, 'Are Directors Trustees? Conflict of Interest and Corporate Morality' (1966) 22 *Business Lawyer* 35. Cf Norwood P Beveridge, 'The Corporate Director's Fiduciary Duty of Loyalty: Understanding the Self-Interested Director Transaction' (1992) 41 *DePaul Law Review* 655.

¹⁰⁴ Marsh, above n 103, 37.

¹⁰⁵ Ibid 39.

¹⁰⁶ Ibid 43.

approved. The interested directors can be counted in a quorum at the meeting of the board of directors.¹⁰⁷

In practice, the application of this statutory requirement is difficult and it is claimed that the Delaware court's approach to Section 144 is perplexing.¹⁰⁸ In *Fleigler v Lawrence*¹⁰⁹ the challenged transaction was an option agreement allowing the company to acquire another company. The transaction was approved by the majority of the shareholders of the acquired company. The dissenting shareholders of the acquired company argued that the approval was unfair as the majority shareholders stood on both sides of the transaction. The defendant officers, directors, and shareholders of the acquired company claimed that the transaction was approved by the shareholders, and according to Section 144, they did not bear the burden of proof. However, the court held that the ratification did not affect the burden of proof as the majority shareholders were not disinterested.¹¹⁰ The court further held that although the statute does not require the disinterested shareholders' approval, it:

[M]erely removes an 'interested director' cloud when its terms are met and provides against invalidation of an agreement 'solely' because such a director or officer is involved. Nothing in the statute sanctions unfairness to [the company] or removes the transaction from judicial scrutiny.¹¹¹

In *Marciano v Nakash*, the court observed that the court in *Fliegler* 'refused to view [S]ection 144 either as completely preemptive of the common law duty of director fidelity or as constituting a grant of board immunity'.¹¹² However, the court in *Marciano* was of the opinion that the approval by disinterested directors or disinterested shareholders provide the defendants with the protection of the business judgment rule.¹¹³ In *Oberly v Kirby*, the court affirmed this:

The key to upholding an interested transaction is the approval of some neutral decision-making body. Under § 144 a transaction will be sheltered from shareholder challenge if

¹⁰⁷ Delaware General Corporation Law § 144(b).

¹⁰⁸ Pinto and Branson, above n 11, 231.

¹⁰⁹ *Fleigler v Lawrence* A.2d 218 (Del, 1976).

¹¹⁰ *Ibid* 221.

¹¹¹ *Ibid* 222.

¹¹² *Marciano v Nakash* 535 A.2d 400 (Del, 1987) 404.

¹¹³ *Ibid* 405 (see footnote no 3).

approved by either a committee of independent directors, the shareholders, or the courts.¹¹⁴

The court in *Cinerama Inc v Technicolor Inc* held that Section 144 did not protect the board with the presumption of the business judgment rule but only shifts the burden to the plaintiff to prove unfairness.¹¹⁵ From these decisions, it may be concluded that if a challenged transaction has complied with the statutory requirements, the burden of proof will be shifted to the plaintiff; however, the Delaware court is still entitled to determine the fairness of the challenged transaction. To evaluate whether the transaction was fair to the company, the court employed the “entire fairness” test in the conflict of interested transactions. The court in *Weinberger v UOP Inc* held that the concept of fairness had both procedural and substantive elements – fair dealing and fair price.¹¹⁶ The former considered how the transaction was structured, negotiated, disclosed and approved.¹¹⁷ The latter examined all related economic and financial factors impacting on the value of a company’s stock.¹¹⁸

Rules governing the duty of loyalty in German law are different from those in US law. As a German company includes the management and supervisory boards, the rules applying to these boards are distinct. Only the management board is empowered to manage the company’s business.¹¹⁹ The members of the management board are prohibited from being engaged on their behalf or on behalf of others in any of the company’s business unless permitted to do so.¹²⁰ Any transactions between the company and a member of the management board must be approved by the supervisory board, not the disinterested directors or the entire management board.¹²¹ The consent given must be only for a specific trade, a specific commercial enterprise, or specific

¹¹⁴ *Oberly v Kirby* 592 A.2d 445 (Del, 1991) 467.

¹¹⁵ *Cinerama Inc v Technicolor Inc* 663 A.2d 1156 (Del, 1995) 1169.

¹¹⁶ *Weinberger v UOP Inc* 457 A.2d 701 (Del, 1983) 711.

¹¹⁷ *Ibid.*

¹¹⁸ *Ibid.*

¹¹⁹ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 76(1).

¹²⁰ *Ibid* § 88; Pierre-Henri Conac, Luca Enriques and Martin Gelter, 'Constraining Dominant Shareholders' Self Dealing: The Legal Framework in France, Germany, and Italy' (ECGI Working Paper No 88/2007, European Corporate Governance Institute, 2007) 12.

¹²¹ Baums and Scott, above n 92, 48.

kinds of transactions.¹²² As in US law, German courts once strictly prohibited self-dealing transactions but later they applied a broader approach called the “general fairness” test.¹²³ This concept was developed under the principle of good faith in the sense used in Section 242 of the German Civil Code.¹²⁴ Nevertheless, as the facts in each case vary, it is difficult to generalise the criteria developed by the courts.¹²⁵

As the supervisory board is not empowered to enter into contracts on behalf of the company, the duty of loyalty of the supervisory board is different from that of the management board. The members of the supervisory board may hold positions on the supervisory boards of another nine companies. Such supervisors have to evenly divide their loyalties between the companies.¹²⁶ To ensure that the supervisors devote their time and energy to all the companies and to reduce the dilemma of multiple loyalties, the law limits their membership to 10 supervisory boards.¹²⁷ Supervisors must disclose their membership of all the companies on which they serve.¹²⁸ The members of the supervisory board can only provide professional services to the company when the consent of the supervisory board is granted.¹²⁹ Multiple loyalties, and resulting conflicts of interest for members of supervisory boards, may occur in other ways. Under co-determination, the members of the supervisory board include labour representatives. A supervisor representing labour faces serious conflicts of interests. For example, when a labour representative participates in the board’s decision on labour policies, or when, as an employee and a member of the union, he or she votes to strike.¹³⁰ In practice, this issue is solved by a compromise among labour representatives and the company. The supervisor is allowed to speak on policies relating to employment but not to participate in voting.¹³¹

¹²² Ibid.

¹²³ Joachim, above n 37, 54.

¹²⁴ Ibid.

¹²⁵ Ibid.

¹²⁶ Ibid 53.

¹²⁷ Ibid; *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 100(2).

¹²⁸ Allison Dabbs Garrett, 'Themes and Variations: The Convergence of Corporate Governance Practices in Major World Markets' (2004) 32 *Denver Journal of International Law and Policy* 147, 166.

¹²⁹ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 114.

¹³⁰ Hopt, above n 46, 1360.

¹³¹ Ibid.

In Thailand, any rules and principles relating to the duty of loyalty have been developed by legislation rather than by the courts as no case on the duty of loyalty of directors of public companies has been brought to the Supreme Court.¹³² Prior to 2008, self-interested transactions in listed companies were mainly regulated by the Public Limited Company Act. The law prohibited company directors from competing with the company's business,¹³³ or purchasing or selling a property to the company unless the approval of the board of directors was given.¹³⁴ The directors were also required to immediately inform the company if they had interests in a contract entered into by the company or held shares in the company or its subsidiaries.¹³⁵ The law recognised the relationship between directors and the company as one between principals and agents involving the fiduciary duties set out in the Civil and Commercial Code.¹³⁶ In 2008, the duty of loyalty was later revised by the Securities Act. The duty of loyalty under Thai securities law can be illustrated as follows:

¹³² Information based on the search engine provided by the Supreme Court website as of March 2012 at <http://www.deka2007.supremecourt.or.th/deka/web/search.jsp>.

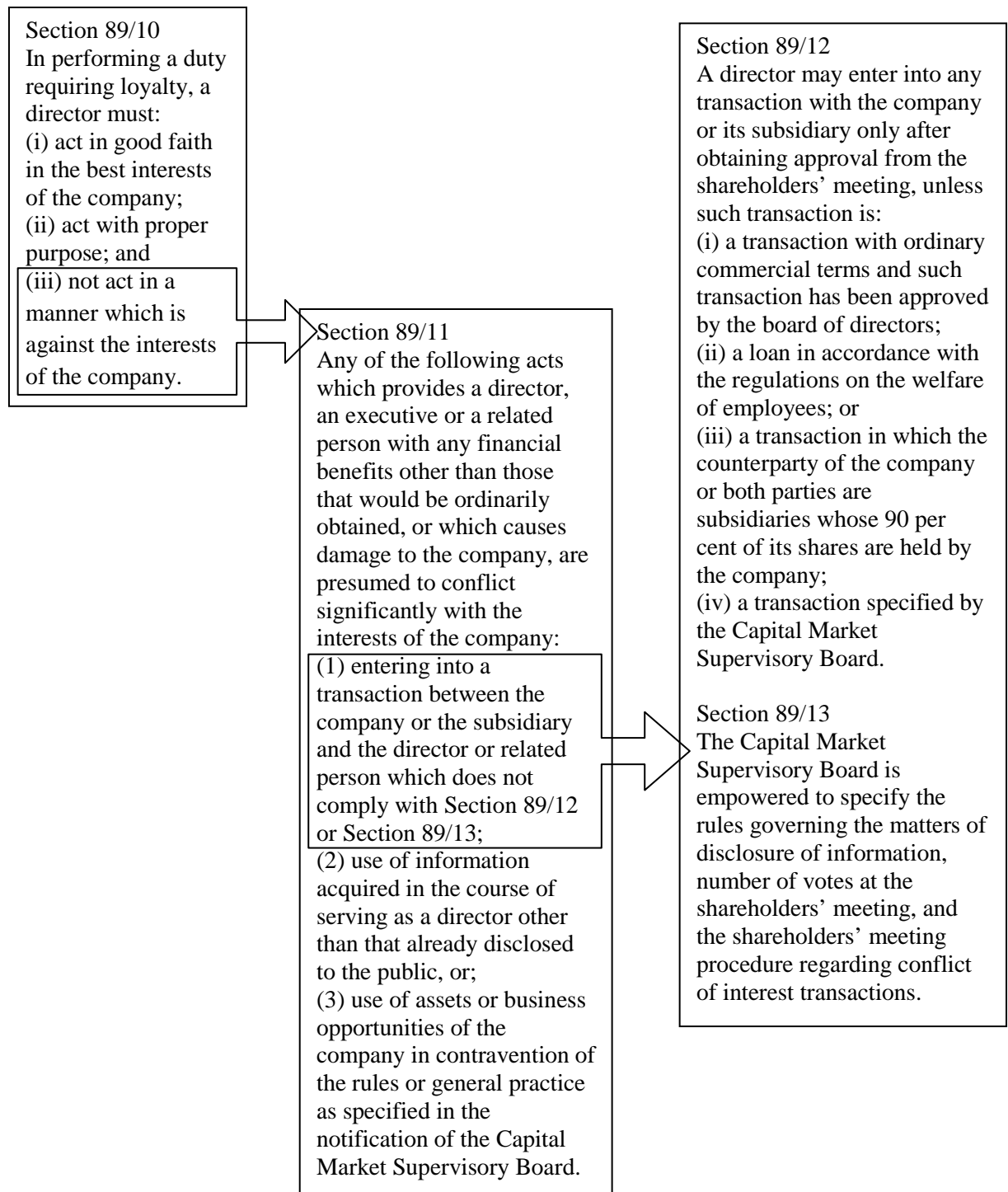
¹³³ Public Limited Company Act B.E. 2535 (1992) (Thailand) s 86.

¹³⁴ Ibid s 87.

¹³⁵ Ibid s 88.

¹³⁶ Ibid s 97.

Figure 5.1 Directors' duty of loyalty under Thai law



Source: Author's compilation

During the course of the interviews, the interviewees were questioned on the duty of loyalty. All of them agreed that due to the limited role of the Thai courts, the duty of loyalty under Thai law has been mainly developed in legislation rather than by judicial decision. One professional independent director commented on the enactment of the revised duty of loyalty:

The new provisions on the duty of loyalty are more like a guideline, or a check list for a company to follow. I understand that the reasons behind this are firstly there is no case law developed on this issue. [This is s]imilar to the duty of care. Secondly, it is likely impossible to impose a clear definition of “loyalty” or “in the interest of the company”. The provisions therefore are in the form of samples of the acts [which are against the interest of the company] to illustrate the scope of the duty of loyalty. The good thing is this method makes the provisions easy for a director to follow.¹³⁷

A Thai academic lawyer affirmed this, saying:

As the Thai court has had no opportunity to draw the scope of “good faith” or “the interest of the company”, the revised provisions will benefit the directors as they will have an idea of which transactions they are not able to enter into or are able to enter into with caution.¹³⁸

A Thai legal practitioner pointed to the power of the Capital Market Supervisory Board to regulate transactions:

The provisions allow the Capital Market Supervisory Board to specify any other transactions which are assumed to conflict with the interests of the company or are required to be approved by the shareholders’ meeting. I find this method suitable for the Thai legal system. Relying on the [Capital Market Supervisory Board] to enact additional rules when necessary is appropriate. The process through the Board is flexible and faster than judicial procedures. The members of the Board are experts in this area. They have a long experience in supervising market activities.¹³⁹

In summary, the laws on the duty of loyalty in the US, Germany, and Thailand are distinctive. US law has changed its approach from prohibiting to permitting conflicts of interest transactions. It has also established a fairness test to determine whether such

¹³⁷ Interview with a professional independent director, Bangkok.

¹³⁸ Interview with an academic researcher, Bangkok.

¹³⁹ Interview with a corporate lawyer, Bangkok.

transactions are fair to the company. German law has also changed. The power to monitor and challenge transactions is left to the supervisory board. The law mainly focuses on issues of the integrity and independence of both the management and supervisory boards. For members of the supervisory board in particular, the law seeks to ensure their loyalty to the 10 companies in which they hold positions. This implicitly accepts conflicts of interests. In Thailand, the concept of the duty of loyalty is less developed. Although Thai corporate legislation has recognised the duty of loyalty, the language is broad. The Supreme Court has never interpreted the provision. Recently, legislation has further particularised the duty of loyalty to facilitate legal compliance. As shown in the above figure, the relevant legislation provides a step-by-step guideline for directors to follow. This is a substitute for the judicial interpretation of the broad statutory language. This approach may be suitable for Thailand where courts have very limited roles.

5.2.4 Avoidance of liability

While US, German, and Thai law imposes duties on directors, it may also allow directors to exclude or reduce their liabilities. This section discusses how directors may seek to protect themselves from liabilities resulting from a breach of duty in the three jurisdictions. The study also focuses on which organ – the board of directors or the shareholders' meeting – is empowered to reduce the directors' liability. This is significant in the Thai context. As discussed in Chapter 2, controlling shareholders generally appoint their family members or acquaintances to sit on the board. They may use their voting power at the shareholders' meeting to waive any liability of the directors they favour.

In US practice, the concept of the indemnification of directors was recognised in the 1950s and has further developed¹⁴⁰ into an expansive approach.¹⁴¹ DGCL in particular explicitly recognises the possibility of the company granting immunity to directors by shifting their liability to the company if a director's actions are in good faith and are

¹⁴⁰ See James J Hanks and Larry P Scriggins, 'Protecting Directors and Officers from Liability – The Influence of the Model Business Corporation Act' (2000) 56 *Business Lawyer* 3.

¹⁴¹ Ibid.

exercised in a manner not opposed to the best interests of the corporation.¹⁴² The indemnification must be granted by: (i) a majority vote of the disinterested directors, or, (ii) a committee of such directors appointed by a majority of the vote of disinterested directors.¹⁴³ Where there is no such director, the opinion of an independent legal counsel or a majority vote of the shareholders will serve the same purpose.¹⁴⁴ Regardless of whether or not the company has the power to indemnify a director, the company is empowered to purchase insurance on behalf of directors against any civil liability.¹⁴⁵ Legislation has come to further extend the power of the company to waive directors' liability for acts of negligence or gross negligence.¹⁴⁶ Section 102(b)(7) of the DGCL states that the certificate of incorporation may contain a provision eliminating or limiting the personal liability of a director to the corporation for monetary damages for the breach of their fiduciary duties as a director. The protection cannot extend to damages for breaches of the duty of loyalty to the corporation or its shareholders where acts are not done in good faith or for intentional misconduct or for transactions from which the director derives an improper personal benefit.¹⁴⁷ The enactment of Section 102(b)(7) followed *Smith v Van Gorkom*.¹⁴⁸ In this case, the board decided to accept a cash-out merger proposal at a significant premium (about 50 per cent above the market price). The court held that although the price was significantly high, the board failed to establish the intrinsic value of the company but accepted the price represented by its chair. Holding the board liable even though the shareholders had received a 50 per cent premium produced a significant reaction in the corporate community.¹⁴⁹ The government of Delaware became concerned that the decision may lead to corporations incorporated in Delaware reincorporating elsewhere.¹⁵⁰ It was argued that the decision had to be reversed to encourage qualified people to serve as directors.¹⁵¹ In practice,

¹⁴² Delaware General Corporation Law § 145(a).

¹⁴³ Ibid § 145(d).

¹⁴⁴ Ibid.

¹⁴⁵ Ibid § 145(g).

¹⁴⁶ Ibid § 102(b)(7).

¹⁴⁷ Ibid.

¹⁴⁸ *Smith v Van Gorkom* 488 A.2d 858 (Del, 1985).

¹⁴⁹ Daniel R Fischel, 'The Business Judgment Rule and the Trans Union Case' (1985) 40 *Business Lawyer* 1437; 'Roundtable: The Legacy of "Smith v Van Gorkom"' (2000) 24 *Directors and Board* 28.

¹⁵⁰ Pinto and Branson, above n 11, 217.

¹⁵¹ Scott J David, 'Would Changes in the Rules for Director Selection and Liability Help Public Companies Gain Some of Private Equity's Advantages?' (2009) 76 *University of Chicago Law Review* 83, 100.

almost every public company incorporated in Delaware exculpates directors from liability in its certificate of incorporation as permitted by Section 102(b)(7).¹⁵²

Unlike US law, German corporate law does not allow a company to exclude or reduce directors' liability. Article 23, Subsection 5, of the *AktG* specifies that the company's articles of incorporation may only be different from the provisions of the Act if the Act explicitly permits this. Articles 93 and 116 specify the duties of the members of the management and the supervisory boards and do not permit companies to exempt members of the boards from these liabilities.¹⁵³ Therefore, no company may reduce the liability imposed by the legislation.¹⁵⁴ However, the company may waive or settle a claim against a director within three years from the date on which the claim was raised¹⁵⁵ but only with the consent of the shareholders in a meeting.¹⁵⁶ Minority shareholders, with at least 10 per cent of the share capital of the company, may object to the waiver or the settlement.¹⁵⁷ German company law does not empower the company to purchase liability insurance on behalf of directors. In practice, directors' liability insurance schemes do not exist in Germany and their liability has not been grouped into the similar professional liability of lawyers, accountants, or auditors.¹⁵⁸ Furthermore, unlike the US practice, the board members of German corporations do not see liability insurance as necessary because, although derivative and class actions are permissible, actions are rarely brought by minority shareholders.¹⁵⁹

Similarly to the German approach, Thai company law does not clearly state whether it is possible to exempt directors from liabilities imposed by it. The general principle of Thai contract law on this issue is Section 151 of the Civil and Commercial Code. It states that juristic acts which are explicitly forbidden by law on account of their being impossible or against public order and morality are null and void. There is no precedent of the Thai Supreme Court in considering whether the law on directors' duties is related to public

¹⁵² Ibid.

¹⁵³ Joachim, above n 37, 64–5.

¹⁵⁴ Ibid.

¹⁵⁵ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 93 sub-s 4.

¹⁵⁶ Ibid.

¹⁵⁷ Ibid.

¹⁵⁸ Joachim, above n 37, 65–6.

¹⁵⁹ Ibid 66.

order or good morals. The provision on directors' liability appears to be a mandatory law that cannot be legally avoided. Section 85 of the Public Limited Company Act and Section 89/7 of the Securities Act requires that the directors must perform their duties in accordance with the law. In addition, the interest of the shareholders may be considered as sufficient public interest because the contract between directors and the company affects large numbers of shareholders. Therefore, it is unlikely that the company and directors, by agreement, can exclude the directors' liability imposed by law. Despite such limitations, the law empowers a majority of the shareholders' meeting or the board of directors to waive the directors' liability if such liability does not result from the directors acting in bad faith or with gross negligence including: presenting false information or concealing material information in the shareholders' meeting; misappropriating or dealing with assets or benefits of the company; and, exploiting assets of the company.¹⁶⁰ Company law does not prohibit the company from purchasing insurance on behalf of the directors. In practice, the number of Thai companies purchasing insurance on behalf of their directors is increasing.¹⁶¹

In comparing the corporate law of the three jurisdictions, only Delaware law allows the company and directors to exclude the duties of directors imposed by law. This appears to recognise the law-and-economic analysis which suggests that the relationship between directors and shareholders is contractual. The parties are therefore able to shape the terms of the contract including terms that are inconsistent with common and statutory law. In German and Thai law, on the contrary, this has not been acknowledged. The interests of shareholders appear to have been considered more significant and they have been more strongly protected. It is therefore not possible to limit directors' liability. The approach which Germany and Thailand have taken to protect minority shareholders may be more suitable for these two jurisdictions than the Delaware one. As companies in Germany and Thailand are mainly dominated by controlling shareholders, the controlling shareholders are able to select someone whom they trust to sit on the board or they may even control the company's business through the shareholders' meeting. If the law further allows the company, shareholders or directors to limit the directors' liability, controlling shareholders and the directors may

¹⁶⁰ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/21.

¹⁶¹ Nitiporn Vitayatem, 'Directors and Officers Liability Insurance' (2000) 25(2) *Insurance Journal* 3, 15.

take undue advantage of the interests of the minority shareholders without being liable to them.

The other significant difference in corporate law in these three jurisdictions is the organ that is authorised to indemnify directors for liability. The practice in Delaware recognises the power of a majority of disinterested directors to limit such liabilities within specified conditions. German law does not empower the board of directors or the supervisory board to waive the directors' liability. The only organ authorised to do so is the shareholders' meeting. Thai corporate law takes a different approach. With limitations, it allows both the majority of the shareholders' meeting and the board of directors to waive the directors' liability.¹⁶² Its approach raises some issues. Firstly, it is questionable whether the interested directors can vote for indemnification. The most relevant provision is Section 1185 of the Commercial and Civil Code. Section 1185 states that in the shareholders' meeting a shareholder who has a special interest cannot vote on such resolution. The directors whose act is indemnified may be considered as having a special interest in the resolution and so cannot vote. Secondly, the law does not distinguish between the power of the board of directors and the shareholders' meeting. It is unclear when the board can consider the indemnification itself or whether it should have the issue considered by the shareholders' meeting. Finally, as pointed out in Chapter 2, Thai companies are mainly controlled by majority shareholders and they tend to appoint those with whom they have a connection to the board. Controlling shareholders may use the shareholders' meeting to ratify the actions of their acquaintances. The only limitation in Thai law applying to ratifications is the acts done in bad faith or with gross negligence.

5.3 Fiduciary duties of controlling shareholders

The previous sections discussed the duties of corporate directors. This section focuses on whether controlling shareholders, under US, German and Thai law, have any obligations towards minority shareholders, and if so, how such obligations are different from those of directors. This issue is significant in the context of Thai companies. As

¹⁶² Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/21.

discussed in Chapter 2, the conflict within a concentrated ownership company is between controlling and minority shareholders, principals and principals, rather than between principals and agents, directors and small shareholders, in US corporations.

It can be argued that generally shareholders have no duties, including fiduciary duties, to other shareholders, as they should be able to exercise their voting rights as they please to pursue their own economic interests.¹⁶³ Controlling shareholders may employ their power for their own benefit in ways that may harm other shareholders.¹⁶⁴ They are able to dominate companies by appointing their family or acquaintances to the board. They also may employ their votes in the shareholders' meeting to force minority shareholders to sell shares in freezeout transactions. Moreover, controlling shareholders may sell their majority shares for a premium price without considering the effect of such sales on other shareholders. So it can be argued that it is necessary to impose a duty on controlling shareholders not to exercise their rights to unfairly damage other shareholders. However, what is considered as "unfair" is not likely to be agreed on.

Unlike transactions between companies and interested directors, related-party transactions between corporations and their controlling shareholders are not regulated in DGCL. The common law therefore plays a significant role in what, if any, the fiduciary duties controlling shareholders owe. In *Sinclair Oil Corp v Levien*,¹⁶⁵ a minority shareholder of Sinven argued that Sinven's dividend policy favoured its controlling shareholders, Sinclair Oil Corporation. The court held that the dividend policy was a strategic decision for the company to make which affected both controlling and non-controlling shareholders. Under the business judgment rule, the court held that it would not interfere except in cases of fraud or gross negligence.¹⁶⁶ In the same case, the shareholders also argue that a contract between a Sinclair subsidiary and Sinven was unfairly administered. Sinclair had breached the contract but Sinven had not received adequate damages. On this issue, the court applied the intrinsic fairness test as the

¹⁶³ *Ivanhoe Partners v Newmont Min Corp* 535 A.2d 1334 (Del, 1987) 1344. The court affirmed that '[i]t is well established law that nothing precludes ... a stockholder from acting in its own self-interest'.

¹⁶⁴ Ronald J Gilson and Jeffrey N Gordon, 'Controlling Controlling Shareholders' (2003–2004) 152 *University of Pennsylvania Law Review* 785, 787.

¹⁶⁵ *Sinclair Oil Corp v Levien* 280 A.2d 717 (Del, 1971).

¹⁶⁶ *Ibid* 720.

parent company, Sinclair, was on both sides of the transaction.¹⁶⁷ Sinclair hence had the burden of proving that the self-dealing transaction was intrinsically fair. As it failed to show that the enforcement of contract was fair to Sinven, it was responsible to the shareholders for any losses.¹⁶⁸ In a later decision, the Delaware Court of Chancery affirmed that 'it does not ... require that directors or controlling shareholders sacrifice their own financial interest in the enterprise for the sake of the corporation or its minority shareholders'.¹⁶⁹ The duty of controlling shareholders is only to act fairly to the corporation and minority shareholders.

The freezeout of minority shareholders is the other common form of controlling shareholder transaction. This may be done to force minority shareholders to sell their stock for unreasonably low prices.¹⁷⁰ In *Weinberger v UOP Inc*, Signal Oil Co held a majority of shares and had six out of 13 directors of UOP, offered US\$21 per share to buy out all shareholders, a 50 per cent premium over the market price. The merger proposal was approved by the majority of the minority shareholders but some minority shareholders brought an action claiming that the merger transaction failed the entire fairness standard. The court ruled that when 'one stands on both sides of a transaction, he has the burden of establishing its entire fairness, sufficient to pass the test of careful scrutiny by the courts'.¹⁷¹ The entire fairness standard consists of both fair dealing and fair price. The former considers how the transaction is structured, negotiated, disclosed and approved.¹⁷² The latter examines all related economic and financial factors attached to the value of a company's stock.¹⁷³ In this case, a feasibility study prepared by two of the UOP directors, who were also directors of Signal, indicated that the value of the shares was up to US\$24. However, the report had never been seen and taken into consideration by the independent directors or minority shareholders of UOP. Applying the fair dealing rules, the court held that the approval of a majority of the minority shareholders was ineffective as they were not aware of the fair value of the shares.¹⁷⁴

¹⁶⁷ Ibid.

¹⁶⁸ Ibid 723.

¹⁶⁹ *Jedwab v MGM Grand Hotels Inc* 509 A.2d 584 (Del Ch, 1986) 589.

¹⁷⁰ The discussion on freezeout transactions is in Chapter 6.

¹⁷¹ *Weinberger v UOP Inc* 457 A.2d 701 (Del, 1983) 710.

¹⁷² Ibid 711.

¹⁷³ Ibid.

¹⁷⁴ The court indicated that there was a duty of candour:

The court in *Weinberger* explicitly affirmed that minority shareholders, similar to controlling shareholders, are entitled to know all material facts before making a decision.

Similar to the Delaware position, a duty in controlling shareholders to minority shareholders is acknowledged by German law. Loyalty (*Treuepflicht*) in the context of German law refers to the close relationship among members of a group, such as the relationship between partners or between family members in a close corporation.¹⁷⁵ Such a relationship exists amongst people in a group where they have an influence on determining the direction of the group. This duty of loyalty does not exist in the context of publicly held corporations. In such corporations each shareholder normally does not have enough shares to control the corporations or determine their decision.¹⁷⁶ In 1976 the issue was raised. In *Audi*, a case was brought by minority shareholders against controlling shareholders on the grounds of the breach of duty of good faith or loyalty.¹⁷⁷ Volkswagen, holding 75 per cent of Audi, had bought a small portion of Audi shares from minority shareholders for DM145 per share. The price was determined by Volkswagen. Two weeks later, Volkswagen bought 14 per cent of Audi's holding from the British-Israeli Bank for DM220 per share. The complaint by the minority shareholders about the difference in the price was rejected on the grounds that controlling shareholders had no duty of good faith or loyalty. The Federal Supreme Court also held that Volkswagen had no duty to reveal its negotiations with the British-Israeli Bank as such an action may have negatively affected the value of Volkswagen's shares. The decision explicitly affirmed that controlling shareholders do not have a duty

One possessing superior knowledge may not mislead any stockholder by use of corporate information to which the latter is not privy. Delaware has long imposed this duty even upon persons who are not corporate officers or directors, but who nonetheless are privy to matters of interest or significance to their company.

Ibid.

¹⁷⁵ Michael Halberstam, *Globalizing Trust? Transferring Anglo-American Minority Shareholder Protections to Civil Law Germany* (2004) Social Science Research Network <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1273067> (unpublished) at 20 March 2012, 35.

¹⁷⁶ *Ibid.* 35–6.

¹⁷⁷ Simon Johnson et al, 'Tunneling' (2000) 90 *The American Economic Review* 22, 25–6.

to the minority shareholders. However, in 1988 the Federal Supreme Court overruled *Audi*.¹⁷⁸

Linotype, a privately held corporation, attempted to merge with D Stempel, a publicly held corporation, and one of its subsidiaries. Under the statutory scheme for merger, the consent of all shareholders was required. Linotype instead used approval from the shareholders' meeting to liquidate D Stempel and transfer D Stempel's assets to itself. Linotype held 96 per cent of the D Stempel shares while minority shareholders held four per cent. One of the minority shareholders of D Stempel brought an action against Linotype claiming that the liquidation of the company had abused his voting rights. The question was whether a parent might dissolve a subsidiary to circumvent statutory merger provisions. The Federal Supreme Court nullified the resolution and affirmed that the majority shareholders had used their voting privilege to the detriment of minority shareholders. *Linotype* and following decisions affirm that controlling shareholders have a duty of loyalty to minority shareholders.¹⁷⁹

In addition to the duty of loyalty among shareholders, German law acknowledges the conflicts of interest arising in the context of corporate groups.¹⁸⁰ Corporate groups are categorised into two types, ie, groups with enterprise agreements and groups without enterprise agreements. For the former type, the enterprise agreements governed by law include a control agreement,¹⁸¹ a profit transfer agreement¹⁸² and a profit pool agreement.¹⁸³ To amend any enterprise agreement, the approval of three-quarters of shareholders in the meeting is required.¹⁸⁴ The law requires the enterprise agreements to

¹⁷⁸ Hwa-Jin Kim, 'Markets Financial Institutions and Corporate Governance: Perspectives from Germany' (1994–1995) 26 *Law & Policy in International Business* 371, 393–4; Halberstam, above n 175, 37–38; Conac, Enriques and Gelter, above n 120, 13–4.

¹⁷⁹ In *Girmes*, the Federal Supreme Court held that, not only majority shareholders, minority shareholders also had a duty of loyalty to other shareholders. See Halberstam, above n 175, 38.

¹⁸⁰ Under the *AktG*, the legally separated enterprises considered as affiliated enterprises are: (i) subsidiary and parent corporations, (ii) controlled and controlling corporations, (iii) members of a group (*Konzern*), (iv) enterprises with cross-shareholdings, and (v) parties to an enterprise agreement. See, *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) §§ 15–19.

¹⁸¹ An agreement in which a company submits to the direction of another company. Ibid § 291(1).

¹⁸² An agreement that a company undertakes to transfer its entire profits to another company. Ibid § 291(1).

¹⁸³ An agreement that a company undertake to pool its profits in whole or in part with the profits of another company. Ibid § 292(1).

¹⁸⁴ Ibid § 293(1).

be inspected by one or more qualified auditors.¹⁸⁵ The management board of the controlled company is required to follow the instructions of the management board of the controlling companies.¹⁸⁶ The directors of the controlling company must exercise the care equal to that of a diligent and conscientious manager,¹⁸⁷ which is the general standard imposed on directors in every public company.¹⁸⁸ If any case is brought against directors alleging a breach of the duty of care, the directors must bear the burden of proof that they have employed the required degree of care.¹⁸⁹ As with other claims relating to breaches of duties, a company may waive or settle a claim against a director within three years from the occurrence of the alleged breach.¹⁹⁰ To waive such a claim, the consent of the minority shareholders in the shareholders' meeting is required.¹⁹¹ Minority shareholders with at least 10 per cent of the share capital may block the vote.¹⁹² In addition, the law requires that a profit transfer agreement must specify the guaranteed annual dividends for minority shareholders,¹⁹³ based on past profitability of the company and its prospective profits.¹⁹⁴ A control or profit transfer agreement must also require a company to purchase the shares of a minority shareholder at an adequate cost,¹⁹⁵ if the minority shareholder chooses so.¹⁹⁶

The German law on a company group extends to *de facto* groups.¹⁹⁷ In the absence of a control agreement, a controlling enterprise is also required by the *AktG* not to use its influence to harm a controlled company.¹⁹⁸ Moreover, the board of a controlled company must make a report to be externally audited and examined by the supervisory board on all the transactions entered with the controlling company as well as on the

¹⁸⁵ Ibid §293b.

¹⁸⁶ Ibid § 308.

¹⁸⁷ Ibid § 309(1).

¹⁸⁸ See *ibid* § 93(1).

¹⁸⁹ Ibid § 309(2).

¹⁹⁰ Ibid § 309(3).

¹⁹¹ Ibid.

¹⁹² Ibid.

¹⁹³ Ibid § 304(1).

¹⁹⁴ Ibid § 304(2).

¹⁹⁵ Ibid § 305(3). The determination of an adequate compensation considers the conditions of the company at the time of approval of shareholders in the meeting granted. This must include interest at the rate of two per cent per annum.

¹⁹⁶ Ibid § 305(1).

¹⁹⁷ Eddy Wymeersch, 'Do We Need a Law on Groups of Companies?' in Klaus J Hopt and Eddy Wymeersch (eds), *Capital Markets and Company Law* (2003) 573, 587.

¹⁹⁸ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 311(1).

advantages and disadvantages of such transactions.¹⁹⁹ If a controlling enterprise causes any damage to a controlled company without compensating it,²⁰⁰ the controlling enterprise, together with its management board, will be liable to the shareholders of the controlled company for any resulting damages.²⁰¹ The board members of the controlled company are also liable if they fail to state that the company has suffered through any disadvantageous transaction and any damages have not been compensated.²⁰² Similarly, the supervisory board of the controlled company is also liable if they have violated the duty to examine the report on relations with affiliated enterprises and to notify the shareholders' meeting on the findings of such disadvantage or damages.²⁰³

Overall, the recognition of a conflicts of interest arising in the context of corporate groups – both *de jure* and *de facto* ones – is to ensure that the interests of all related parties, including minority shareholders, are protected.²⁰⁴

Unlike the Delaware and German practice, the duty of controlling shareholders has not been acknowledged in Thailand. There is no specific legislative provision governing the duty of controlling shareholders to minority shareholders. As well, the Supreme Court has not had to consider the duty of controlling shareholders because minority shareholders never bring an action against controlling shareholders on the grounds of a breach of duty of good faith or loyalty. The contractual relationship among shareholders in a company is different from a partnership in which all members agree to establish a business organisation with a view of sharing profits and being entitled to act on behalf of others. The relationship between the managing partners and the other partners is governed by the law on principals and agents.²⁰⁵ The same provisions do not apply to the relationship between controlling shareholders and minority shareholders. All shareholders are free to promote their own interests by voting their own shares. Furthermore, even if controlling shareholders vote in a way harmful to minority

¹⁹⁹ Ibid § 312(1).

²⁰⁰ Ibid § 371(3)

²⁰¹ Ibid § 317(1).

²⁰² Ibid § 318(1).

²⁰³ Ibid § 318(2).

²⁰⁴ Wymeersch, above n 197, 588. The author also observed '[a]s was ably stated by Hommelhoff and Druey, the German system is far from satisfactory. It is based on a valid theoretical concept – that of balancing the profits and losses – but is unworkable in practice'.

²⁰⁵ Civil and Commercial Code as amended until Code (No 18), B.E. 2551 (2008) (Thailand) s 1042.

shareholders, such an action is not unlawful nor a breach of duty as the controlling shareholders have a right to do so.

During the interviews, the interviewees were questioned about their views on controlling shareholders in Thai companies. An investor pointed out:

I think the reason of why the sense of ownership in a Thai company is very strong is [controlling shareholders] see the company as their personal asset. They build up their own company from the ground. Then they put the company into the market. They use their own capability and connection to maintain the company's growth. So, if we are going to put a limitation on their voting right, they may not understand why they cannot exercise their right in the way they wish. It will be very interesting to see, if there is a case brought by minority shareholders against controlling shareholders, how the court will justify the duty of controlling shareholders towards minority shareholders.²⁰⁶

An independent director agreed with this view, saying:

In Thailand, controlling shareholders have the belief that they are the owners of the companies. They therefore are able to sell their shares in any way they please. If there is no rule imposing the limitation of their rights, they can freely manage their wealth. The critical issue is how to balance the interests of both controlling and minority shareholders.²⁰⁷

In summary, from the experience of the three jurisdictions, the existence and the scope of the duty of controlling shareholders is defined by the courts rather than the legislation. The US Supreme Court employs the concept of “fairness” as the grounds to establish the scope of duty. The German Federal Court applies the idea of “loyalty” as a base to acknowledge the duty of controlling shareholders. The Thai court, as noted, has had no opportunity to have consideration in this issue. Thailand may pay more attention to the duty of controlling shareholders because, as mentioned in Chapter 2, the major conflict within Thai companies is between controlling and minority shareholders. However, as the findings reveal, Thai business and legal practitioners believe that controlling shareholders are allowed to exercise their rights to pursue their own financial interests.

²⁰⁶ Interview with an investor, Bangkok.

²⁰⁷ Interview with a professional independent director, Bangkok.

Under German law, the relationship among companies in the same group is regulated. This is to ensure that the interests of all parties are protected. Given a similar business structure, Thailand may consider developing a law governing the conflicts of interest in corporate groups. Control of the transactions within the group is important, as when such transactions are transparent, controlling shareholders cannot easily use the business group structure to tunnel the company's assets to controlling shareholders.

5.4 Conclusion

The concept of “trust” or “faith” exists in both common and civil law jurisdictions in respect of directors' duties. The directors have a duty to act with care and in the best interests of the company. However, the law on the directors' duties in Germany and Thailand is less developed than that in the US. In the US, the common law courts play a significant role in defining the directors' duties while in civil law countries they are mainly found in legislation. The common law system provides for incremental changes to the law based on changing business and social contexts. Due to the limited number of cases taken to court in civil law jurisdictions, courts also play a limited role in applying and interpreting the law on fiduciary duties. Regarding the duty of controlling shareholders, both German and Delaware laws acknowledge its existence. This duty has not been affirmed by the Thai court or legislation. The findings show that Thai practitioners disagree that controlling shareholders have a duty to minority shareholders, as controlling shareholders should be able to exercise their voting rights as they please. This reflects a widely held acceptance that the founding and controlling shareholders are the legitimate owners of the company. Thai corporate law reform should pay more attention to this issue as the major conflict within its concentrated ownership companies is between controlling and minority shareholders, rather than directors and shareholders. While Thailand has attempted to adopt US concepts of directors' duties, it is not possible for regulatory agencies or the courts to give a clear content and scope to them. Only the courts are able to define the scope through their decisions on a case-by-case basis. Given the limited role of the Thai court, it is questionable whether such adopted legal rules will be applied in practice. The study considers how the laws and practices in

the three jurisdictions protect minority shareholders in specific contexts which directly affect minority shareholders.

Chapter 6

Minority Shareholders' Protection in Specific Contexts

- 6.1 Introduction
- 6.2 Changes in control
 - 6.2.1 Mergers
 - 6.2.1.1 Mergers made by agreement
 - 6.2.1.2 Asset acquisitions
 - 6.2.2 Hostile takeovers
 - 6.2.2.1 Proxy contests
 - 6.2.2.2 Hostile bids
 - 6.2.3 Freezeouts
- 6.3 Related-party transactions
- 6.4 Conclusion

6.1 Introduction

The previous chapters considered the laws and practices in the US, Germany and Thailand relating to the management and proprietary rights of minority shareholders and the duties of boards of directors and controlling shareholders. This chapter focuses on the transactions that are related to those who have control over the company – the board of directors and controlling shareholders. These transactions are mergers, asset acquisitions, takeovers, freezeouts, and related-party transactions. These issues are important as these transactions have significant impacts on companies and on the interests of minority shareholders. The rules and regulations in the three jurisdictions which seek to protect minority shareholders in these specific contexts are reviewed. Provisions governing changes in control transactions and related-party transactions are considered.

6.2 Changes in control

A change in control within a company may occur when existing shareholders acquire additional shares and gain sufficient voting power to dominate or replace the current management. Outsiders can acquire control with, or without, the consent of the

company's incumbent board. These changes directly impact on minority shareholders' interests. New controlling shareholders or management may set new business policies that are significantly different from previous ones. Alternatively dissenting minority shareholders may sell their shares but this option may not always be fair as the share price may decline sharply due to new management. There may be a lack of market liquidity. This section describes how laws and regulations in the US, Germany, and Thailand deal with corporate control transactions.

6.2.1 Mergers

When an outsider – generally a corporation – and the management of corporation decide to merge their corporations into one firm, this can be carried out in different ways. One is to merge the corporations and another is to acquire the assets of one from the other. These processes raise many issues, including whether there are fair procedures for the approval of such transactions; whether the shareholders of both corporations receive adequate information about the transaction before making a decision to approve or oppose it; whether they receive a fair share including a share in the premium for control; and, whether there is a remedy for dissenting shareholders in such a transaction. This section focuses on how the law in the three jurisdictions deals with the rights of minority shareholders in mergers and asset acquisitions.

6.2.1.1 Mergers made by agreement

In negotiating a merger agreement the directors must act in good faith and in an informed manner, otherwise, they may breach their duties. The details of the directors' duties have been discussed in the previous chapter. This section focuses on merger provisions in the three jurisdictions and related issues, including the role of the board of directors, notice requirements, shareholder voting, and any remedy for dissenting shareholders.

To effectuate a merger under Delaware General Corporate Law (“DGCL”), the acquirer and target boards of directors firstly negotiate a merger agreement.¹ After agreement has been reached, the boards of both the acquirer and target companies must provide their shareholders with copies of the merger agreement and call shareholders’ meetings.² The law requires the boards to mail notices of the meetings and all relevant documents to the shareholders at least 20 days before the meetings.³ In addition, both the acquirer and target companies are subject to the Securities and Exchange Commission (“SEC”) disclosure rules. The details of the merger must comply in the form of a proxy statement on Schedule 14A.⁴ To approve such a transaction, a majority vote of the shareholders is required.⁵ DGCL does not prohibit interested shareholders from voting on this issue.⁶ Unless required in its certificate of incorporation, no vote of shareholders of the acquirer is necessary if the merger has no effect on such company; for instance, the merger does not amend the certificate of incorporation of the acquirer.⁷ No vote of the shareholders of both the acquirer and the target is required if the acquirer corporation owns at least 90 per cent of the stocks of the target company.⁸ After the shareholders’ meeting approves the transaction, the companies must file a certificate of merger with the Secretary of State to effect the merger.⁹ All the assets, rights, and liabilities of the target corporation become the acquirer’s.¹⁰ Dissenting shareholders generally have a right to have the value of their shares appraised by a petition filed in the Chancery Court. The Court determines the value of their stocks. However, such a right is not provided to shareholders in a company that is listed on an exchange or has more than 2,000 shareholders.¹¹ The main purpose of this provision is to facilitate mergers rather than provide remedies for dissenting shareholders. In respect of more

¹ Delaware General Corporation Law § 251(a). The details of the merger agreement are governed by Delaware General Corporation Law § 251(b).

² Ibid § 251(c).

³ Ibid.

⁴ See Securities Exchange Act of 1934 Rule 14A.

⁵ Ibid.

⁶ Delaware General Corporation Law § 251(c).

⁷ Ibid § 251(f).

⁸ Ibid § 253. This type of merger is known as a “short form” merger.

⁹ Ibid § 251(d).

¹⁰ Ibid § 259.

¹¹ Ibid § 262(b).

widely held or listed companies, the absence of an appraisal right relies on the function of the market to reflect the appropriate value of shares.¹²

The significant issue concerning merger transactions is the use of special committees. The power of the board to create and authorise a special committee to approve mergers is permitted.¹³ Without a special committee, as discussed in Chapter 5, if the transaction involves controlling shareholders or when the majority of the directors are interested, the transaction is subjected to the entire fairness test. The role of a special committee generally begins from the negotiation of the merger transaction. The main purpose of having a special committee is to show that the transaction is entirely fair to the company and its shareholders.¹⁴ A special committee also provides a legal benefit as it shifts the burden of proving entire fairness from the defendant company to the plaintiff shareholders.¹⁵ The Delaware Court shifts the burden of proof when it is clearly shown that the members of a special committee are independent, and disinterested.¹⁶ They must also exercise their power in an informed and active manner.¹⁷ Importantly, the special committee must have real bargaining power. On behalf of minority shareholders, the committee must have the power to negotiate the transaction and even to veto the transaction.¹⁸

While US practice relies on the use of special committees to ensure the fairness of the mergers, the German practice employs independent qualified public accountants to examine the transactions. In Germany, a merger transaction is governed by a special law, the *Umwandlungsgesetz* of 1994 [Transformation Act] (“*UmwG*”), instead of the general corporate law. The *UmwG* was reformed in 1994 by the *Gesetz zur Bereinigung*

¹² Unlike the revised Model Business Corporation Act of 2002, in recognition that the market may not reflect the true value of a company’s shares, the Act provides that the market exception is not applicable to a merger that involves 20 per cent of shareholders or an insider group that controls 25 per cent of a board of directors. Model Business Corporation Act 2002 § 13.02(b)(4).

¹³ Delaware General Corporation Law § 141(c).

¹⁴ Jeffrey A Chapman and Benjamin W James, ‘The Use of Special Committees in Mergers and Acquisitions’ (2008) 42(3) *Texas Journal of Business Law* 315, 316.

¹⁵ *Ibid* 326.

¹⁶ See, eg, *In re Tele-Communications Inc Shareholders Litigation* A.2d, 1 (Del Ch, 2005). See also William T Allen, ‘Independent Directors in MBO Transactions: Are They Fact or Fantasy?’ (1990) 45 *Business Lawyer* 2055.

¹⁷ *Ibid*.

¹⁸ See, eg, *Kahn v Tremont Corp* A.2d, 1 (Del Ch, 1996).

des Umwandlungsrechts [German Transformation Law Amendment Act]. The purpose of the amendment was to unify various statutes on mergers and provide better remedies to stakeholders.¹⁹ The *UmwG* governs the combination of two or more business entities – mergers – and other forms of reorganisation, such as a transaction in which an entity splits up its assets and transfers them to two or more entities.²⁰ Initially, the management boards of the acquirer and target companies negotiate and draft terms of the contract.²¹ To protect all shareholders, the law requires the draft terms to be examined by independent qualified public accountants.²² The opinion of the chartered accountants is to ensure the fairness of the merger.²³ The boards of both corporations then provide the shareholders of any related entities with reports describing the details of, and the reasons for, the merger and a report prepared by qualified accountants prior to the meeting to ensure that shareholders have sufficient information to make their decisions.²⁴ A majority vote of shareholders of the combined entities is necessary to pass the resolution.²⁵ Dissenting shareholders may take action to invalidate the resolution authorising the merger subject to limitation.²⁶ For example, an action on the grounds that the consideration given to shareholders is unreasonable is not allowed.²⁷ Regarding the role of worker participation and the supervisory board, the *UmwG* does not require the approval of the supervisory board to merger transactions as the merger does not affect individual employees. Under the German Civil Code, no employment contracts will be cancelled due to a change of ownership.²⁸ The acquirer must also take over any employment contracts on the same conditions.²⁹

¹⁹ Arndt Stengel, 'The New German Business Transformation Act' (1995) 6(3) *International Company and Commercial Law Review* 86, 86.

²⁰ *Ibid* 88.

²¹ *Ibid* 89–90.

²² *Ibid*.

²³ Their opinion was usually based on the guidelines for the valuation of enterprises issued by the Institut der Wirtschaftsprüfer in Deutschland e.V. (Institute of Chartered Accounts or IDW). Herbert Harrer and Mark Devlin, 'Fairness Opinions in Germany and the United States of America' (2008) 23 *Journal of International Banking Law and Regulation* 603.

²⁴ Stengel, above n 19, 89–90.

²⁵ *Ibid*.

²⁶ *Ibid*.

²⁷ *Ibid* 90–91.

²⁸ *Umwandlungsgesetz* of 1994 [Transformation Act] (Germany) § 324 in conjunction with *Bürgerliches Gesetzbuch* [Civil Code] (Germany) § 613a.

²⁹ *Ibid*.

Thai law is similar to German law. It seeks to minimise potential conflicts of interest by relying on the opinion of a financial advisor. Merger transactions under Thai law are governed by the Public Limited Companies Act. Two or more companies can amalgamate into one by the agreement of the meetings of shareholders of the relevant companies.³⁰ The companies must submit notices of the meeting and all relevant documents, including the details of the merger agreement and the reports of a registered financial advisor to the shareholders 14 days prior to the meeting.³¹ A vote of not less than three-quarters of shareholders of each company is required to pass the resolution.³² If some shareholders object to the resolution, the company must offer to buy their shares at the market price at the time of amalgamation.³³ The dissenting shareholders must decide whether to accept such an offer within 14 days of the date of receiving the proposal, otherwise they will become shareholders in the amalgamated company.³⁴

6.2.1.2 Asset acquisitions

In addition to mergers, a corporation may acquire another firm by purchasing the substantial assets. The cost of asset transfers is higher than that of a statutory merger as there are additional costs in transferring the physical assets of the target corporation to the acquirer. In exchange for the target's assets, the acquirer company can offer its stock, cash or some combination of cash and other securities.

Under Delaware corporations law, after negotiation between the boards of the acquirer and target companies is concluded, the board of the target corporation must call a meeting of shareholders for their approval.³⁵ The notice of the shareholders' meeting must be sent to the shareholders at least 20 days before the meeting.³⁶ A majority vote of shareholders of only the target corporation is required to approve the terms of the agreement.³⁷ DGCL does not prohibit interested shareholders from voting on this issue.

³⁰ Public Limited Company Act B.E. 2535 (1992) (Thailand) s 146 para 1.

³¹ SET Notification No Bor.Jor./Por.24-00.

³² Public Limited Company Act B.E. 2535 (1992) (Thailand) s 146 para 1.

³³ Ibid s 146 para 2.

³⁴ Ibid s 146 para 2.

³⁵ Delaware General Corporation Law § 271(a).

³⁶ Ibid.

³⁷ Ibid.

The law also does not give appraisal rights to dissenting shareholders to seek determination of the value of their shares unless the company's certificate of incorporation specifies otherwise.³⁸ In practice, similarly to a merger transaction, the company establishes a special committee to negotiate and approve asset transfer agreements. The Delaware court considers whether the members of the special committee are independent, disinterested, and active, informed, and importantly, whether the special committee has real bargaining power. If so, the burden of proof of the entire fairness of the transaction is shifted to the plaintiff shareholders.

In Germany, the procedures for asset acquisitions and mergers are similar. Asset transfer agreements are governed by the *UmwG*. The management boards of the transferor and transferee negotiate and draft the terms of the contract.³⁹ The draft terms must be examined by independent qualified public accountants.⁴⁰ Prior to the meeting, the board must submit the draft terms of the transfer transaction and the report prepared by independent, qualified public accountants to the shareholders.⁴¹ A vote of the majority shareholders of all entities is required to validate the draft terms.⁴² The law prohibits dissenting shareholders from bringing an action against the resolution authorising the transformation on the grounds that the consideration given to them is unreasonable. Similar to mergers, the *UmwG* does not require the approval of the supervisory board because the asset transfer agreement does not affect individual employees. No employment contracts will be cancelled in the change of ownership and the transferor must take over the existing work contracts and conditions.⁴³

In Thailand, asset transfer transactions are mainly governed by the listing rules of the Stock Exchange of Thailand.⁴⁴ The transferor and transferee companies must have a financial advisor, approved by the Thai SEC, to give opinions on the transaction,

³⁸ Ibid § 262(c). Similar to the revised Model Business Corporation Act of 2002 §§ 13.02(a)(3), 13.02(b)(1).

³⁹ Stengel, above n 19, 89–90.

⁴⁰ Ibid.

⁴¹ Ibid.

⁴² Ibid.

⁴³ *Umwandlungsgesetz* of 1994 [Transformation Act] (Germany) § 324 in conjunction with *Bürgerliches Gesetzbuch* [Civil Code] (Germany) § 613a.

⁴⁴ The Securities Act empowers the SEC to impose the rules on the acquisition or disposal of assets transactions. See Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/29; SEC Notification No Tor.Jor. 20/2551; SET Notification No Bor.Jor./Por.21-01.

including its reasonableness and the fairness of the price and conditions.⁴⁵ The advisor also provides a recommendation to the shareholders on whether they should agree with the transfer.⁴⁶ The company will then have to supply the shareholders with relevant information and an opinion from the financial advisor at least 14 days prior to the meeting.⁴⁷ A vote of at least three-quarters of shareholders attending the meeting, excluding interested shareholders, is required to pass the resolution.⁴⁸ Unlike a merger transaction, the law does not require the companies to purchase shares from dissenting shareholders.

Of the three jurisdictions, Thai law on mergers and asset acquisitions provides more suitable protection in companies with concentrated ownership. Under Delaware and German law, the majority approval of shareholders in both acquirer and target companies is required. On the other hand, Thai law requires a supermajority vote to approve merger and asset transfer agreements. Due to the concentrated shareholding of Thai companies, a vote of three-fourths of the shareholders is more appropriate than a simple majority vote because the higher voting threshold makes it more possible for minority shareholders to successfully object to the transactions. Regarding conflicts of interests, the law in the three jurisdictions deals with these issues in different ways. Delaware law does not require a review of the merger or asset acquisition agreements by independent experts. In practice, however, the company employs a special committee to negotiate and approve the transactions. The role of the Delaware court in the use of special committees is significant. If the defendant company fails to show that the special committee acts on behalf of minority shareholders, the defendant company bears the burden of proof of the entire fairness of the transaction. German and Thai laws approach this differently. The management of German and Thai companies must provide the opinion of an independent financial expert to shareholders for their consideration. One may argue that the requirement of a second opinion from independent financial experts is beneficial to minority shareholders as it helps them in making a more informed decision. Others may question the independence of such financial experts.

⁴⁵ SET Notification No Bor.Jor./Por.21-01 article 30.

⁴⁶ Ibid.

⁴⁷ Ibid.

⁴⁸ Ibid article 34.

Unlike the US practice, where the court plays a significant role in examining the independence of the special committee, German and Thai laws only requires financial experts to be qualified or registered. In Thailand, the financial advisors must be those whose names appear on a list approved by the Thai SEC. To date, there are 68 financial institutions and 305 authorised financial advisors.⁴⁹ The Thai SEC generally grants approval for three to five years.⁵⁰ The financial advisors are required to maintain their independence. However, in practice, the independence of the financial advisors may not be ensured. As a financial analyst pointed out:

The SEC Notification imposes some requirements to ensure the independence of the financial advisors. In practice, however, it is arguable whether they are truly independent. Although financial advisors must be registered with the SEC, in reality, those who pay for them are the companies who hire them to give an advice. Given this conflict of interests, the influence of the company over the financial advisors is inevitable. This situation is similar to the relationship between the company and its auditor. In practice, the company ensures the independence of the advice given by the financial advisors by having two or more financial advisors to give an opinion on the same issue.⁵¹

In respect of remedies for dissenting shareholders, the laws in the three jurisdictions rely on the market value of a company's shares rather than allowing shareholders to ask the court to determine the value.

6.2.2 Hostile takeovers

The above techniques are deployed when the board of directors of the target company is in favour of the transaction. If not, the acquisition of control is generally described as a “hostile takeover” or “*feindliche Übernahme*” in German and “*kub rum kit ja karn*” in Thai. A hostile takeover is a feature of the market for corporate control. As noted in Chapter 2, Manne suggested that the market for corporate control was represented in a connection between corporate managerial efficiency and the market price of the shares

⁴⁹ Securities and Exchange Commission, *List of Financial Advisors Approved by the Office of the SEC* (2011) Securities and Exchange Commission <www.sec.or.th/securities_issuance/fa.doc> at 20 March 2012.

⁵⁰ Ibid.

⁵¹ Interview with a financial analyst, Bangkok.

of that company.⁵² When the share price of a company falls due to poor management, then outsiders, in the belief that the drop is due to poor management, may take over company to use its assets more effectively.⁵³ To acquire the control against the opposition of the management of the target company, the outsiders will have to seek to gain sufficient voting power in the target company by proxy contests or tender offers in US terminology.

6.2.2.1 Proxy contests

In the US proxy contests are largely regulated by federal legislation relating to corporate securities. It allows the shareholders of a target company to select two slates of candidatures: one from the target's incumbent management and the other from outside the existing management. In the US, the proxy contest for corporate control is widely used. The proxy rules first appeared in the Securities Exchange Act of 1934. The Act was revised in 1992 when hostile acquisitions became a major phenomenon. The regulation of proxy contests seeks to enable shareholders to make decisions on an informed basis. To communicate with the shareholders, the bidder may forward the proxy statement to acquire shareholders' votes to the address of shareholders provided by the target company.⁵⁴ The target company may retain the shareholders' list and itself transmit the bidder's materials to shareholders at the challenger's expense.⁵⁵ In practice, the target company generally sends out the challenger's materials rather than providing it with the shareholders' list.⁵⁶ The bidder is also required to ensure accuracy of the information in the materials to be delivered to the shareholders.⁵⁷

Unlike the US, proxy fights in Germany are extremely rare.⁵⁸ A departure from German corporate practices occurred in February 2010 when the proxy fight at Infineon

⁵² Henry G Manne, 'Mergers and the Market for Corporate Control' (1965) 73(2) *The Journal of Political Economy* 110, 112.

⁵³ Ibid 113.

⁵⁴ Securities Exchange Act of 1934 Rule 14d-5.

⁵⁵ Ibid.

⁵⁶ Jeffrey Bauman, Elliott Weiss and Alan Palmiter, *Corporations Law and Policy: Materials and Problems* (5th ed, 2003) 1099.

⁵⁷ Securities Exchange Act of 1934 Rule 14a-9.

⁵⁸ Theodor Baums and Kenneth E Scott, 'Taking Shareholder Protection Seriously? Corporate Governance in the United States and Germany' (2005) 17(4) *Journal of Applied Corporate Finance* 44,

Technologies AG, a DAX30 constituent company, over the appointment of a member of its supervisory board took place.⁵⁹ Hermes, a British fund manager, filed a shareholder countermotion calling on shareholders not to re-elect a former member of the supervisory board and proposing an alternative candidate.⁶⁰ Hermes' stake in Infineon Technologies AG was less than three per cent, but due to its influence on other investors as a fund manager, 27.5 per cent of the vote was cast against the re-election of the former supervisory board member.⁶¹ This event signals to German companies that foreign investors may introduce more aspects of shareholder activism and use shareholders' meetings to install new management. Despite this possibility, German law has no provisions on the completeness or accuracy of information provided to shareholders in proxy contests.⁶²

In Thailand, similarly to German practice, proxy fights rarely happen.⁶³ During the course of the interviews for this thesis, one corporate lawyer explained that 'given the concentrated ownership, it is likely to be impossible for outsiders or existing shareholders to gather sufficient votes to overcome the power of majority shareholders'.⁶⁴ Despite this, the Securities and Exchange Act ("Securities Act") was amended in 2008 to regulate proxy solicitation.⁶⁵ As indicated in Chapter 4, the purpose of the introduction was so that Thai company law would be consistent with international standards. This provision is to ensure that, before proxies are granted, shareholders must

59; Heinz-Dieter Assmann, Barbara Lang and Rolf Sethe, 'The Law of Business Associations' in Mathias Reimann and Joachim Zekoll (eds), *Introduction to German Law* (2005) 152.

⁵⁹ Asha Doogah and Frank J Cifarelli, 'Current Corporate Governance Trends in Germany' (2010) 1(41) *Governance & Proxy Review* <http://www.altmangroup.com/gpr/vol1_issue41.html> at 20 March 2012; *Infineon Proxy Contest Opens New Chapter in German Corporate Governance* (2010) Manifest – The Proxy Voting Agency <<http://blog.manifest.co.uk/2010/01/2829.html>> at 20 March 2012.

⁶⁰ Ibid. See also Hermes Equity Ownership Services, 'Hermes Equity Ownership Services Files Shareholder Proposal on Behalf of its Clients Regarding the Election to the Supervisory Board at the AGM of Infineon AG on 11 February 2010' (Hermes press Release 19 January 2010).

⁶¹ Ibid. See also Vereinigung Institutionelle Privatanleger eV, *Annual General Meeting of Infineon Technologies AG on February 11th 2010 – Proposal of a Shareholder for the Election of a Supervisory Board Member and Counter Motion According to §§127, 126 AktG Regarding Item 7 on the Agenda* (2010) Manifest – the Proxy Voting Agency <<http://www.hmb.ag/files/!!vipcountermotion2010.pdf>> at 20 March 2012.

⁶² Oliver Rieckers and Gerald Spindler, 'Corporate Governance: Legal Aspects' in Jan Pieter Krahn and Michael H Schellenger (eds), *The German Financial System* (2004) 378.

⁶³ Information based on the interviews with an officer of the Securities and Exchange Commission of Thailand, Bangkok, and an investor, Bangkok.

⁶⁴ Interview with a corporate lawyer, Bangkok.

⁶⁵ The enactment of Securities and Exchange Act (No 4) B.E.2551 (2008).

receive sufficient and accurate information.⁶⁶ The law only defines the meaning of “solicitation” and otherwise authorises the regulator to make further detailed rules.⁶⁷ The Thai SEC is still in the process of drafting the regulations.⁶⁸

6.2.2.2 Hostile bids

In addition to proxy contests, a bidder may employ a hostile tender by offering to buy stocks directly from shareholders. Usually this will be at a price substantially higher than the market price. This process carries significant risks to the bidder, as it has no opportunity to confirm the value of the business of the target company. The cost of a hostile takeover is expensive. The outcome is however unpredictable. While the bidder is arranging sufficient financing for specialised advice and share purchases, the target may seek out a white knight to make a higher bid. If the bidder still wishes to pursue the takeover, a white knight’s offer might have to be topped. For the shareholders of the target company, although they may receive share premiums for their shares over the market price, they are uncertain whether, and to whom, they should sell their shares. On the one hand, they may believe that the shares are worth more than the bidders’ offer so that they may decide to reject the offer. On the other hand, they may fear that if the bidder acquires sufficient stocks to control the company, the prices of any remaining stocks will fall. As indicated, during the takeover period, the board of the target company may attempt to protect their interests by setting up them, such as seeking out a white knight, selling the company’s significant assets, or repurchasing the company’s shares. Defensive tactics are controversial. The incumbent board members may employ defensive tactics to protect their own interests instead of protecting the company and shareholders’ interests.⁶⁹

⁶⁶ *Inside SEC* (2010) Security and Exchange Commission <http://www.sec.or.th/internetradio/inside_sec_detail.jsp?categoryID=CAT0000508&lang=th&radioId=00039> at 20 March 2012.

⁶⁷ Securities and Exchange Act B.E. 2535 (Thailand) s 89/31.

⁶⁸ The hearing on draft regulations was taken until 20 June 2008. SEC News No 37/2008. Until now the draft regulations have not come into effect.

⁶⁹ See Bauman, Weiss and Palmiter, above n 56, 1117–1195.

United States

In the US, shareholders receive considerable protection under federal securities law. The Williams Act in 1968 further amended Sections 13 and 14 of the Securities Exchange Act of 1934. The Williams Act requires any person who makes a tender offer for more than five per cent of a corporation's stocks, to file with the SEC, a statement containing the information on the bidder, the source of funds and the bidder's purpose and plans within 10 days of the purchase.⁷⁰ Once proposed, the offer must remain open for 20 business days during which shareholders who tender their shares may also withdraw them.⁷¹ This is to allow shareholders to accept any competing bids subsequently offered. When the bidder offers to acquire only some but not all shares, it must accept the tendered shares from each shareholder on a *pro rata* basis.⁷² Moreover, if the bidder increases the bidding price, the increased price will also apply to all tendering shareholders, including those who previously tendered their shares before the increase.⁷³ Importantly, the law prohibits material misstatements, material omission, fraudulent practice and deceptive practices throughout the transaction.⁷⁴ In the late 1970s to the 1980s, hostile tender offers became a significant phenomenon and received considerable attention from scholars, politicians, and regulators. One of the significant economic and legal debates was whether a hostile takeover benefited a target company and the whole economy.⁷⁵ Although many researchers affirm the advantages of hostile takeovers, they also result in considerable corporate restructuring and massive layoffs.⁷⁶ This influenced a majority of states to adopt legislation allowing takeover defence, known as anti-takeover legislation.⁷⁷ They raised the issue of whether these laws were valid because of their conflict with the federal law – the Williams Act. The Supreme

⁷⁰ Securities Exchange Act of 1934 § 14(d)(1).

⁷¹ *Ibid* §§ 14e-1, 14(d)(5).

⁷² *Ibid* § 14(d)(6).

⁷³ *Ibid* § 14(d)(7).

⁷⁴ *Ibid* § 14(e).

⁷⁵ See, eg, Jonathan R Macey, 'State Anti-Takeover Legislation and the National Economy' (1988) 1988 *Wisconsin Law Review* 467; Michael L Wachter, 'Takeover Defense When Financial Markets are (Only) Relatively Efficient' (2002–2003) 151 *University of Pennsylvania Law Review* 787.

⁷⁶ See Roberta Romano, 'The Political Economy of Takeover Statutes' (1987) 73 *Virginia Law Review* 111.

⁷⁷ *Ibid*.

Court upheld the validity of the state laws. It affirmed that they regulated the internal affairs of corporations and were not affected by the Williams Act.⁷⁸

In Delaware, the anti-takeover law is imposed in Delaware General Corporation Law Section 203. When an acquirer passes the 15 per cent shareholding threshold, the law bars any combination between it and the company for a period of three years. The exceptions to this prohibition are: (i) a takeover which is approved by the target board before the takeover bid occurs; (ii) an acquirer who gains more than 85 per cent of the company's shares in a single offer; and, (iii) an acquirer who receives approval from the target board and a two-third vote of disinterested shareholders – minority shareholders who do not tender their shares. However, in practice, it is difficult for the acquirer to fit within the exceptions. If the target board disagrees with the bid, it may seek a white knight to acquire some of the company's shares to prevent the acquirer from passing the 85 per cent threshold. Also, the shareholders who do not tender their shares at the beginning are unlikely to grant approval to the bidder.

In response to a hostile takeover, a target's management may defend its control of the corporation. The board's action raises issues over the responsibility of the board. One may consider that the directors have a conflict of interest because they may adopt defensive tactics to protect their positions. It becomes necessary to observe whether such decisions are fair to the company. Others may view that the defensive tactics are similar to other business decisions so that the directors' exercise of discretion is protected by the business judgment rule. The Delaware Supreme Court considered the management's responsibility for defensive tactics in *Unocal Corp v Mesa Petroleum Co.*⁷⁹ In this case, the court held that the business judgment rule was applicable in the context of a takeover. The board had a duty to make a decision in good faith, on an informed basis, and in the best interests of the company.⁸⁰ To be protected by the business judgment rule, the board had to prove that it had reasonable grounds to believe that the takeover bid would have an adverse effect on the corporation.⁸¹ In addition, the

⁷⁸ *CTS Corp v Dynamics Corp of America* 457 US 624 (1982).

⁷⁹ *Unocal Corp v Mesa Petroleum Co* 493 A.2d 946 (Del, 1985).

⁸⁰ *Ibid* 954.

⁸¹ Such effects include inadequacy of the price offered, the nature and timing of the offer and the impact on stakeholders. *Ibid* 955

board had to show that a defensive measure was reasonable to the threat posed.⁸² Later, in *Revlon*, the court held that when multiple bidders for a corporation made similar offers, the directors must treat all the bidders equally and remain active to ensure that the shareholders would obtain the best price possible for their shares.⁸³ The *Revlon* case, however, did not give a clear answer as to whether the management could pursue another business plan when it considered that the shareholders did not benefit from the sale of the company. The court in *Time* affirmed that, although the offer was made, the board had no obligation to sell a company.⁸⁴ The board's decision, in good faith and with reasonable investigation to expand the business through merger with another corporation, was also protected by the business judgment rule.⁸⁵ In *Paramount Communications Inc v QVC Network Inc*,⁸⁶ the court ruled that, even after the board had entered into a merger agreement with a corporation, if there were another offer proposed by another corporation, the board was also obliged to critically examine such offer with due care and on an informed basis to consider which offer would provide higher benefits for shareholders.⁸⁷ The court further stated that in the sale or change of control transactions, the court would not second-guess the decision of the directors – the business judgment rule – but would consider whether the decision was within the range of reasonableness.⁸⁸

Germany

As indicated, hostile takeover bids are not common in Germany.⁸⁹ This is partly because of the limited number of potential targets, the structural character of German corporations, and the role of banks as large proxy holders.⁹⁰ As Frank and Mayer

⁸² Ibid.

⁸³ *Revlon Inc v MacAndrews & Forbes Inc* 506 A.2d 173 (Del, 1986).

⁸⁴ *Paramount Communications Inc v Time Inc* 571 A.2d 1140 (Del, 1989) 1151.

⁸⁵ Ibid 1152.

⁸⁶ *Communications Inc v QVC Network Inc* 637 A.2d 34 (Del, 1994).

⁸⁷ Ibid 47–8.

⁸⁸ Ibid 45.

⁸⁹ For a discussion on German hostile tender offers, see Roland Donath, 'On the Way to US-Style Hostile Tender Offers in Germany? – The European Attempt to Harmonize the Takeover Law and its Impact on German Company Law' (1994) 1 *Annual Survey of International and Comparative Law* 91.

⁹⁰ Theodor Baums, 'Takeover vs Institutions in Corporate Governance in Germany' (Paper presented at the Oxford Law Colloquium, University of Oxford, the United Kingdom, 10–11 September 1992) 4–9; Theodor Baums, 'Corporate Governance in Germany – System and Recent Developments' (Paper presented at the Corporate Governance Reform, Stockholm, Sweden, 10 December 1993) 22.

observed, large German corporations are not widely held but are concentrated in the hands of families or company groups.⁹¹ Such companies are also linked through pyramid and cross-shareholding patterns that make them difficult to break down the control within company groups. Besides, as indicated in Chapter 4, the voting rights of small investors are generally exercised by German banks as proxy holders. It is thus easy for the bank to prevent hostile takeovers. The management boards also prefer to have banks acquire a controlling block in their companies, as this can be an effective means of protecting acquirer hostile takeovers.⁹² As a result, mergers are generally negotiated among large controlling shareholders rather than through public hostile takeovers. Additionally, although a bidder may be able to acquire the majority share of a target company, it may not be able to control the company due to statutory limitations.

Under the *AktG*, as described earlier, the shareholders cannot directly appoint the management board but half of the supervisory board, which will then appoint the management board. The new controlling shareholders therefore have to remove the shareholder representatives on the supervisory board and elect their candidates. This is difficult in practice because, to remove such members before their terms expire, a vote of more than 75 per cent by shareholders is required.⁹³ Half of the supervisory board's members – labour representatives – cannot be removed. Besides, these labour representatives may not see a hostile takeover as advantageous to them and their work council and may attempt to oppose the bidder.

The public attention on a hostile takeover came to Germany in 2000 when Vodafone offered a takeover bid to shareholders of Mannesmann.⁹⁴ Unlike other German companies, Mannesmann's shares were highly dispersed and mainly held by foreign

⁹¹ Julian R Franks and Colin Mayer, 'Ownership and Control of German Corporations' (2001) 14(4) *Review of Financial Studies* 943; see also Julian R Franks, Colin Mayer and Hannes F Wagner, 'The Origins of the German Corporation – Finance, Ownership and Control' (2006) 10(4) *Review of Finance* 537.

⁹² Theodor Baums, 'Should Banks Own Industrial Firms? Remarks from the German Perspective' (Speech delivered at the Meeting of the Studiecentrum Ondernemingsgroepen/Centre d'étude des groupes d'entreprises, Brussels, 29 January 1992) 7.

⁹³ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 103(1).

⁹⁴ For a history of takeovers in Germany, see William Underhill and Andreas Austmann, 'Defence Tactics' in Jennifer Payne (ed), *Takeovers in English and German Law* (2002) 87–8.

investors.⁹⁵ In November 1999 Vodafone proposed to swap its shares for shares of Mannesmann; however, the proposal was rejected by the Mannesmann management board.⁹⁶ Then Vodafone offered the swap plan directly to Mannesmann's shareholders. The foreign investors tended to be in favour of Vodafone while local investors were not.⁹⁷ Mannesmann sought a white knight but could not find one. As indicated, generally German banks are one of the main barriers to hostile takeovers. However, in this case, the banks played no role. Mannesmann did not have a strong relation with its house bank, Deutsche Bank.⁹⁸ In February 2000 Vodafone and Mannesmann reached an agreement to swap shares.⁹⁹ In January 2004 criminal actions were brought against six persons – the former CEO, the members of the non-executive compensation committee and a former employee of Mannesmann – for breaching their duty of loyalty.¹⁰⁰ The supervisory board was charged with approving over €60 million as awards and pension enhancements to former Mannesmann board members.¹⁰¹ The former CEO himself received approximately €15 million as an “appreciation reward”. It was claimed that the compensation committee breached its duty as it had approved inappropriate payments and such payments were not in the interests of the company.¹⁰² The former CEO was accused of bribery as an appreciation reward was given in exchange for his support of the takeover. The Regional Court ruled that, although the size of the payouts was not approved in the interests of Mannesmann, the payouts did not constitute criminal conduct, as the prosecution claimed.¹⁰³ Finally, in November 2006 the prosecutor decided to drop the charge for an agreement by the six defendants to pay the Federal

⁹⁵ Martin Höpner and Gregory Jackson, 'An Emerging Market for Corporate Control? The Mannesmann Takeover and German Corporate Governance' (MPIfG Discussion Paper No 01/4, Max-Planck-Institut für Gesellschaftsforschung, 2001) 26.

⁹⁶ Ibid 27.

⁹⁷ Ibid 39.

⁹⁸ Ibid 31.

⁹⁹ Ibid 39.

¹⁰⁰ Peter Kolla, 'The Mannesmann Trial and the Role of the Courts' (2004) 5(7) *German Law Journal* 829, 832.

¹⁰¹ Ibid.

¹⁰² Max Philipp Rolshoven, 'The Last Word? – The July 22, 2004 Acquittals in the Mannesmann Trial' (2004) 5(8) *German Law Journal* 935, 938.

¹⁰³ Ibid 939–40; *Deutsche Bank Chief walks free in Mannesmann Trial* (2006) European Social Survey <http://www.europeansocialsurvey.org/index.php?view=details&id=3256&option=com_eventlist&Itemid=326> at 20 March 2012.

Republic and charities a total of €5.8 million.¹⁰⁴ Unsurprisingly, the takeover and trial had received considerable public attention.

The Mannesmann case reflects not only concern over excessive executive remuneration¹⁰⁵ but also concern over the change in German takeover regulations, the German Code of Conduct for Takeovers of 1995.¹⁰⁶ The Code was created to secure the reputation of Germany as a centre of finance and to ensure the transparency and equal treatment of all participants.¹⁰⁷ It also imposed requirements for takeover offers, including the details required in such offers in order to provide sufficient information to shareholders of a target company.¹⁰⁸ The Code was only recommendations of good practice.¹⁰⁹ It neither contained any binding legal norms nor had legislative origin.¹¹⁰ In practice, less than 35 per cent of listed companies complied with it.¹¹¹ The Mannesmann incident led to demands for compulsory takeover procedures.¹¹² The government responded in a draft law in 2000 and a revised draft in 2001.¹¹³ One of the core principles to be incorporated in the law by the draft law was the neutrality rule.¹¹⁴ This rule did not allow the management to use any defensive tactics against a tender offer, leaving any decisions to the shareholders.¹¹⁵ At the same time, a draft EU Takeover

¹⁰⁴ Jean J Du Plessis and Otto Sandrock, 'The German System of Supervisory Codetermination by Employees' in Jean J Du Plessis et al (eds), *German Corporate Governance in International and European Context* (2007) 132–3.

¹⁰⁵ Johnson observed:

Unlike their American counterparts, German executives do not have golden parachutes and many of them do not own substantial stakes in the companies that they run. After the takeover by Vodafone, Mr. Esser [the CEO of Mannesmann] will lose much of the social prestige and power that came with running one of the largest German corporations, and he will be out of a job. It seems ironic that a German CEO who will not benefit from a golden parachute accomplished exactly what most American CEOs with large buyout clauses would hope to do in the same situation.

Benjamin W Johnson, 'German Corporate Culture in the Twenty-First Century: The Interrelation Between the End of Germany Inc. and Germany's Corporate Capital Gains Tax Reform' (2002) 11 *Minnesota Journal of Global Trade* 69, 89.

¹⁰⁶ See, eg, Höpner and Jackson, above n 95.

¹⁰⁷ Karl-Hermann Baumann, 'Takeover in Germany and EU Regulation Experience and Practice' in Klaus J Hopt et al (eds), *Comparative Corporate Governance: The State of the Art and Emerging Research* (1998) 660.

¹⁰⁸ Ibid.

¹⁰⁹ Ibid.

¹¹⁰ Ibid.

¹¹¹ Ibid 662.

¹¹² Ibid.

¹¹³ Höpner and Jackson, above n 95, 46.

¹¹⁴ Ibid.

¹¹⁵ Ibid.

Directive was submitted to the European Parliament but it was rejected partly because it did not give sufficient recognition to co-determination.¹¹⁶ The German takeover law was promulgated in 2001.¹¹⁷ It did not adopt the neutrality rule. Under the law, before any takeover bids occur, a majority of three-quarters of the shareholders' meeting, with the approval of the supervisory board, may put in place defensive measures for up to 18 months in order to protect against takeover bids.¹¹⁸ After a takeover bid is made, the management may only apply defensive tactics with the approval of the supervisory board.¹¹⁹ The revised EU Takeover Directive was eventually adopted in 2006.¹²⁰ The underlying rationale is a common capital market for the EU. The Directive requires adoption of the neutrality rule for management as the default rule for member states.¹²¹ Germany opted out of the requirement and retained the rights for management to take defensive measures if empowered to do so by shareholders.¹²² This approach can be seen as resistance to leaving German companies entirely exposed to market control.¹²³

The *Wertpapiererwerbs- und Übernahmegesetz* of 2001 [Securities Acquisition and Takeover Act] lays down detailed procedures for takeover bids. To acquire the shares of a target company, an offerer must submit its decision to make an offer on the internet and through an electronic information dissemination system to BaFin,¹²⁴ the Federal Financial Supervisory Authority, and the management board of the target company.¹²⁵ The board of management must then forward the documents to the company's work council.¹²⁶ After that, the offerer must prepare to offer documents containing the details of the offerer, the offer, the offerer's business plan, and the offerer's financial position

¹¹⁶ Baums and Scott, above n 58, 60; see also John W Cioffi, 'Corporate Governance Reform, Regulatory Politics, and the Foundations of Finance Capitalism in the United States and Germany' (2006) 7(6) *German Law Journal* 532, 554–6.

¹¹⁷ Ibid.

¹¹⁸ *Wertpapiererwerbs- und Übernahmegesetz* of 2001 [Securities Acquisition and Takeover Act] (Germany) § 33(2).

¹¹⁹ Ibid § 33(1).

¹²⁰ Curtis J Milhaupt and Katharina Pistor, *Law and Capitalism: What Corporate Crises Reveal about Legal Systems and Economic Development Around the World* (2008) 81.

¹²¹ Ibid.

¹²² Ibid.

¹²³ Patrick C Leyens, 'German Company Law: Recent Developments and Future Challenges' (2005) 6(10) *German Company Law* 1407, 1416.

¹²⁴ *Bundesanstalt für Finanzdienstleistungsaufsicht*. The discussion on the authorities of BaFin is in Chapter 7.

¹²⁵ *Wertpapiererwerbs- und Übernahmegesetz* of 2001 [Securities Acquisition and Takeover Act] (Germany) § 10(1), (4)–(5).

¹²⁶ Ibid § 10(5).

for BaFin approval.¹²⁷ After the approval is granted, the documents can be distributed to shareholders.¹²⁸ The shareholders of the target company have four to 10 weeks depending on the offer's condition to accept the offer.¹²⁹ If the offerer adjusts the offer conditions, the acceptance period will be extended by two weeks.¹³⁰ In the case of a partial offer, the acceptance must be considered on a *pro rata* basis.¹³¹ If there are any competing offers, the acceptance period of the first offer will be extended to the acceptance period of the competing offers.¹³² The board of management and the supervisory board must issue a statement responding to the offers to the shareholders without undue delay.¹³³ If material information in the offer document is incorrect, the shareholders having accepted the offers are able to claim for any damages from the offerer.¹³⁴

Thailand

In Thailand, there are hostile tender offers but they are not as common as in the US.¹³⁵ Those interviewed as part of the research for this thesis were asked about the limited number of hostile tender offers in Thailand. They pointed out that most Thai companies are owned by controlling shareholders and so it is almost impossible to acquire sufficient votes to outvote the existing controlling shareholders.¹³⁶ Despite such obstacles, the number of takeover bids increased during 1997-1998.¹³⁷ The 1997 financial crisis saw a large number of foreign companies acquire equity in Thai companies.¹³⁸ After 1999 the number of hostile takeover bids has significantly

¹²⁷ Ibid § 11.

¹²⁸ Ibid § 14.

¹²⁹ Ibid § 16.

¹³⁰ Ibid § 21.

¹³¹ Ibid § 19.

¹³² Ibid § 22.

¹³³ Ibid § 27.

¹³⁴ Ibid § 12.

¹³⁵ Kittipong Uraepatanapong, 'Hostile Takeover Defensive in Thailand and the US Compared' (2005) *October Banking and Finance Journal* 240, 240.

¹³⁶ Interviews with a professional independent director, Bangkok, an officer of the Stock Exchange of Thailand, Bangkok, and an academic researcher, Bangkok.

¹³⁷ See Securities and Exchange Commission, *Takeover Statistics* (2010) Securities and Exchange Commission <http://www.sec.or.th/infocenter/report/Content_0000000141.jsp?categoryID=CAT0000007> at 20 March 2012.

¹³⁸ Prema-chandra Athukorala, 'FDI in Crisis and Recovery: Lessons from the 1997–98 Asian Crisis' (Working papers in trade and development No 2003/04, Division of Economics, Research School of

reduced.¹³⁹ One hostile takeover bid received considerable public attention in 2005 when a close friend of the former prime minister, Taksin, announced hostile bids for two leading Thai newspaper companies.¹⁴⁰ The bids raised fears that the government may interfere in press freedom.¹⁴¹ Eventually, due to resistance from journalists and the public, the bids were withdrawn by the bidder himself.¹⁴²

Hostile tender offers are governed by the Securities Act and the regulation of the Thai SEC.¹⁴³ To provide investors with information on the changes in major shareholdings, when any person acquires, or disposes of shares which are any multiple of five per cent of the total number of voting rights, they must report such transactions to the Thai SEC.¹⁴⁴ The law requires any person who offers purchase securities which represent 25, 50, or 75 per cent of the total voting rights in a company to make a tender offer for all the securities.¹⁴⁵ The information in the tender offer form prepared by an authorised financial advisor must not be misleading, incomplete or inaccurate.¹⁴⁶ Once the tender offer is made, it must remain open for at least 25 to 45 consecutive business days,¹⁴⁷ during which shareholders who have tendered their shares can cancel that tender.¹⁴⁸ The offering price must not be less than the highest price paid for shares by the offerer during the six months prior to the date of submitting the tender offer to the Thai SEC.¹⁴⁹ When a target company receives a tender offer, it must appoint a financial supervisor registered with the Thai SEC to prepare a statement making a recommendation about

Pacific and Asian Studies & Asia Pacific School of Economics and Management, Australian National University, 2003) 10.

¹³⁹ Securities and Exchange Commission, above n 137.

¹⁴⁰ For details on the Thai media, see Ubonrat Siriyuvasak, *Who Owns the Asian Media: Thailand Media Report* (2006) Campaign for Popular Media Reform <<http://www.scribd.com/doc/48214561/UBONRAT-Thailand-media-report>> at 20 March 2012.

¹⁴¹ See, eg, Tunyawat Chaitrakulchai, 'Marketing Strategy: Lesson From Grammy Taking Over Matichon', *Manager* (Bangkok), 2005; *Grammy Withdrew the Takeover, Reduced its Shareholding to 20%* (2003) Bangkokbiznews <<http://www.bangkokbiznews.com/2005/special/takeover/take13.pdf>> at 29 September 2011; *Kimeng did not Realise the Strong Persistence from Public* (2003) Bangkokbiznews <<http://www.bangkokbiznews.com/2005/special/takeover/take15.pdf>> at 29 September 2011.

¹⁴² Ibid.

¹⁴³ For a discussion on tender offer regulation in Thailand, see Bradley J Gordon, 'Recent Development: Revised Tender Offer Regulations in Thailand' (1995) 36 *Harvard International Law Journal* 541.

¹⁴⁴ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 246.

¹⁴⁵ Ibid s 247; Capital Market Supervisory Board Notification No TorJor. 12/2554 clause 4.

¹⁴⁶ Ibid clause 19.

¹⁴⁷ Ibid clause 24.

¹⁴⁸ Ibid clause 31.

¹⁴⁹ Ibid clause 36.

the offer and submit it to the shareholders within 15 business days.¹⁵⁰ To ensure fair treatment among shareholders, for six months after purchasing shares in a tender offer, the offerer must not acquire any securities of the company at a higher price or on better terms than those acquired in the tender offer.¹⁵¹ This is to preserve to all shareholders the premium for control. For one year after the purchase, the offerer is also required to take actions proposed in the offer unless approved by a vote of not less than three-fourths of a shareholders' meeting and notification to the Thai SEC.¹⁵²

Different defensive tactics against a hostile bid can be employed. For instance, the board may propose the shareholders' meeting to approve a capital increase to dilute the shares of the bidder. The board may distribute core assets of the company so that the company cannot operate functionally. The board may purchase an unnecessary property at an unreasonably high price. Also the board may create golden parachutes. This requires the company to provide the board members with significant benefits if their employment is terminated. The purpose of these tactics is to make a hostile bid difficult. They considerably increase the cost of a takeover. The Thai SEC is strongly opposed to defensive tactics.¹⁵³ It sees these tactics as employed by controlling shareholders or the board to retain their controlling power.¹⁵⁴ Their actions may affect the interests of minority shareholders as the bidder may wish to replace the current management in order to improve company performance.¹⁵⁵

The view of the Thai SEC is reflected in the latest revised version of the Securities Act. The law requires defensive tactics against a hostile bid can be employed only with the approval of the shareholders' meeting.¹⁵⁶ To obtain approval for such a transaction, the board must express its opinion in the notice of the shareholders' meeting, including the

¹⁵⁰ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 250; Capital Market Supervisory Board Notification No TorJor. 40/2552.

¹⁵¹ Capital Market Supervisory Board Notification No TorJor. 12/2554 clause 48.

¹⁵² Ibid.

¹⁵³ Securities and Exchange Commission, *Takeover ... Your Choice* (2008) Securities and Exchange Commission <http://www.sec.or.th/investor_edu/info_media/article/manager/manager067_040851.pdf> at 20 March 2012, 2.

¹⁵⁴ Ibid.

¹⁵⁵ Ibid.

¹⁵⁶ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 250/1. The common defensive tactics include acquisition or disposal of material assets; creation of debts; and, payment of extraordinary interim dividends. Capital Market Supervisory Board Notification No TorChor. 6/2552 clause 2.

reasonableness of the transaction, and any benefits from it, whether the price and conditions are fair, and a recommendation to the shareholders on how to vote.¹⁵⁷ Without such approval, the board's acts do not bind the company and the board members themselves may be liable for damages to a third person.¹⁵⁸

In summary, although hostile takeovers are not common in Germany and Thailand, there are laws governing these transactions. Thailand, in particular, has legislated for procedures to ensure that all shareholders can respond to proxy contests and takeover bids on an informed basis. Advice from a financial expert is also provided to assist the shareholders in making decisions. Anti-takeover provisions are also established in Thai legislation. A significant difference between the three jurisdictions is the power of the board of directors to employ defensive tactics. Delaware state law authorises boards to do so and considers such decisions to be within the business judgment rule. On the other hand, in Germany and Thailand, the board is empowered to use defensive mechanisms only when approved by a shareholders' meeting. Reserving power to the shareholders is more suitable for Thailand's circumstances than leaving the decision to the board's discretion. This is because, due to the limited case law, the scope of directors' duties under Thai law is unclear.¹⁵⁹ Without certain guidelines on the extent to which the board can use defensive tactics, the board may employ all possible tactics to resist a takeover. Additionally, without market discipline, there is no external pressure on underperforming boards. Despite the rights provided, it is likely to be impossible for minority shareholders to block the directors' proposals even when they disagree with the defensive tactics due to the highly concentrated shareholding structure.

6.2.3 Freezeouts

After the acquirer obtains sufficient shares to control a target company, it may seek to privatise the company by buying out remaining shareholders. There are several ways for them to achieve this. The most common is the cash out merger in which the controlling

¹⁵⁷ Ibid clause 3.

¹⁵⁸ Securities and Exchange Act B.E. 2535 (Thailand) s 250/1.

¹⁵⁹ Minority shareholders barely bring an action challenging the decision made by the board of directors. The details on shareholders' litigations will be discussed in Chapter 7.

shareholder seeks to cash out the other shareholders' equity interests.¹⁶⁰ The controller may create a new corporation ("Newco") and transfer all of its shares in the target company to Newco. Then the controller has the boards of the target company and Newco to agree to a merger agreement with the terms that the shareholders of the target company will receive cash for their shares. This technique is known as a "freezeout".

Freezeouts raise significant policy issues. On the one hand, they involve conflicts of interest and unfairness to minority shareholders. Controlling shareholders can set the terms of the merger agreement without any participation from non-controlling shareholders. They may attempt to keep the market price of the shares low to make the premium offered to minority shareholders below the actual benefit. Dissenting minority shareholders may also be reluctant to take any action for the determination of a fair price as they see the cost of such an action is higher than the benefit they will receive. On the other hand, controlling shareholders do not always treat minority shareholders unfairly. Easterbrook and Fischel pointed out that freezeouts were expensive.¹⁶¹ The bidder must determine both the cost of the premium over the market price paid to frozen minority shareholders, and whether the company will profitably operate after the transfer of control.¹⁶² In economic terms, freezeouts increase the value of the company's assets as they reduce a number of costs. When the company goes private, firstly, the agency cost is eliminated, or considerably reduced, as there is no separation between ownership and control.¹⁶³ Secondly, freezeouts reduce the costs associated with being a public or listed company, and also avoid high regulatory scrutiny by the governmental regulatory agency or the market supervisor.¹⁶⁴ Given these different issues, this section focuses on whether the laws in the three jurisdictions allow controlling shareholders to compel remaining shareholders to sell their shares and how the laws protect such shareholders.

¹⁶⁰ Arthur M Borden, *Going Private* (2009) § 3.02.

¹⁶¹ Frank H Easterbrook and Daniel R Fischel, 'Corporate Control Transactions' (1982) 93 *Yale Law Journal* 698, 705.

¹⁶² *Ibid.*

¹⁶³ *Ibid* 706. The discussion on agency costs is in Chapter 2.

¹⁶⁴ See 'Guidelines on Going Private' (1981) 37 *Business Lawyer* 313, 321–325.

Under DGCL, when one corporation owns at least 90 per cent of another company's shares, the former may merge the latter into itself or may merge two corporations into a third corporation.¹⁶⁵ The approval of only the board of the company holding 90 per cent of the shares is required.¹⁶⁶ Dissenting shareholders have a right to seek a fair price by filing a petition in the Chancery Court, the right to appraisal.¹⁶⁷ However, small shareholders are unlikely to do so. As Eisenberg explained:

[Appraisal] is always technical; it may be expensive; it is uncertain in result, and, in the case of a publicly held corporation, is unlikely to produce a better result than could have been obtained on the market; and the ultimate award is taxable.¹⁶⁸

Alternatively, the dissenting shareholders may seek to invalidate the merger agreement by arguing that it is unfair. As mentioned in Chapter 5, the court in *Weinberger v UOP Inc* applied the entire fairness test to a transaction when a party stands on both sides. The controller bears the burden of proving that the merger agreement is fairly constructed and that the consideration provided to minority shareholders is fair.

Under German law, when a bidder acquires not less than 95 per cent of the target company, the offerer can apply to the court for the transfer of the remaining shares to it in exchange for payment of fair compensation.¹⁶⁹ Only the Regional Court of Frankfurt am Main has the authority to decide on the application.¹⁷⁰ To ensure equal treatment of shareholders, the compensation given to the remaining shareholders must be similar to that offered in the takeover bid.¹⁷¹ Monetary consideration can always be employed as an alternative compensation.¹⁷² An application for transfer of the shares must be filed within three months after the end of the acceptance period of the takeover bid.¹⁷³ After the application is accepted, the Regional Court will publish in the newspapers advertisements.¹⁷⁴ The Regional Court considers the application on the grounds that the

¹⁶⁵ Delaware General Corporation Law § 253.

¹⁶⁶ Ibid.

¹⁶⁷ Ibid § 262.

¹⁶⁸ Melvin Aron Lisenberg, 'The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking' (1969) 57 *California Law Review* 1, 85.

¹⁶⁹ *Wertpapiererwerbs- und Übernahmegesetz* of 2001 [Securities Acquisition and Takeover Act] (Germany) § 39a(1).

¹⁷⁰ Ibid § 39a(5).

¹⁷¹ Ibid § 39a(3).

¹⁷² Ibid.

¹⁷³ Ibid § 39a(4).

¹⁷⁴ Ibid § 39b(2).

offerer has provided credible evidence that he holds shares representing at least 95 per cent.¹⁷⁵ The decision of the Regional Court can be appealed to the Higher Regional Court of Frankfurt am Main.¹⁷⁶ The decision of the Higher Regional Court cannot be appealed.¹⁷⁷

In Thai law, unlike Delaware and German law, there is no provision allowing the bidder to buy out the equity interests of the remaining shareholders.¹⁷⁸ The only possible method of acquiring the remaining shares is to delist the company from the stock market. In this process, the company must appoint a financial advisor, who is approved by the Thai SEC with the approval of the independent directors, to make a recommendation to the remaining shareholders and to inform the board of directors in resolving to delist the shares.¹⁷⁹ The company must then submit a notice of the meeting and an explanation to the shareholders not less than 14 days prior to the date of the meeting.¹⁸⁰ Not less than seven days prior to the date of the shareholders' meeting, the company and the financial advisor registered with the Thai SEC must make a presentation to the shareholders.¹⁸¹ To pass a resolution, a vote of not less than three-fourths of the total shares is required.¹⁸² Shareholders with more than 10 per cent of the shares, however, can object to the resolution.¹⁸³ This reflects the policy that if the bidder cannot obtain more than 90 per cent of the company's shares, the resolution to delist the company may be blocked by remaining shareholders. Unlike the Chancery Court of Delaware or the Regional Court of Frankfurt am Main there is no specialist court to review the process.

Of the three jurisdictions, only Thai law does not facilitate controlling shareholders to buy out the equity interests of the remaining shareholders, unless, as pointed out, the company is delisted. Although the omission protects minority shareholders, it is

¹⁷⁵ Ibid § 39b(3).

¹⁷⁶ Ibid.

¹⁷⁷ Ibid.

¹⁷⁸ For a detailed study, see Issara Vimomrat, *Adoption of Squeeze Out Concept in Thailand* (M Laws Thesis, Chulalongkorn University, 2010).

¹⁷⁹ SET Regulation Bor.Jor./Phor.01-00 article 4(1).

¹⁸⁰ Ibid article 4(6).

¹⁸¹ Ibid article 4(4).

¹⁸² Ibid article 4(5).

¹⁸³ Ibid.

arguable whether this approach is suitable. As pointed out by Easterbrook and Fischel, freezeouts benefit the target company as they increase the value of its assets. Besides, if there is a guarantee that minority shareholders will receive their control premium at a fair value, prohibiting controlling shareholders from buying the equity interests of the remaining minority shareholders may put an unnecessary burden on controlling shareholders. When a shareholder becomes almost a sole proprietor by holding not less than 90 or 95 per cent of the company shares and decides to pursue a business decision, the law should facilitate the privatisation of the company. Although a company can delist from the market, this process is time consuming and expensive, including the costs of appointing a financial advisor and holding a shareholders' meeting. To balance the interests of controlling and minority shareholders, Thailand may consider adopting provisions to facilitate the controlling shareholders to acquire the remaining shares including judicial review and approval of the transactions.

6.3 Related-party transactions

One of the most contentious issues relating to corporate governance is how to protect minority shareholders from being exploited by those who control a corporation, including directors, and controlling shareholders, or both. These controllers can use their power to tunnel resources out of a company in various ways, such as excessive compensation, transfer pricing, and self-dealing transactions.¹⁸⁴ Transactions relating to directors are discussed in the previous chapter. This section focuses on transactions in which the controlling shareholders, directly or through other entities, enter into contracts with the corporation. How the laws in the three jurisdictions govern related-party transactions are considered by focusing on how such transactions may be approved.

The common law of Delaware only requires the approval of shareholders or the board of directors to permit transactions between a corporation and its directors. In other kinds of related-party transactions such an approval is not required. Minority shareholders may,

¹⁸⁴ For a detailed research, see Simon Johnson et al, 'Tunneling' (2000) 90 *The American Economic Review* 22.

however, challenge the transaction as failing the entire fairness standard.¹⁸⁵ Though the shareholders' approval is not required, related-party transactions are subject to SEC regulations and stock exchange listing rules. SEC regulations impose significant disclosure requirements. Those regulations define related-party transactions as any transactions which exceed US\$120,000 and in which related persons have or will have a material interest.¹⁸⁶ The law considers a shareholder with more than five per cent of the company's shares to be a related person.¹⁸⁷ The details required to be disclosed include the name of the related person; the interest held; the approximate monetary value of the related person's interests in the transaction.¹⁸⁸ The company must also describe its policies and procedures for the ratification of any related-party transactions.¹⁸⁹ For companies listed on the NYSE, the listing rules require the transactions to be reviewed by the company's audit committee.¹⁹⁰ The committee should determine both whether the transactions are in the best interests of the company and whether the relationship of conflict should be continued or eliminated.¹⁹¹

Similar to US law and practice, minority shareholders in a German company are not empowered to review related-party transactions. Under the *AktG*, the approval of the supervisory board is required for related-party transactions between members of the management board and the company¹⁹² but not for transactions between the company and dominant shareholders.¹⁹³ Instead of empowering the shareholders to directly review related-party transactions, German law focuses more on governing processes within a corporate group and relies on internal control mechanisms. As mentioned in Section 5.3, the law on company groups is intended to ensure that the interests of all related parties, including minority shareholders, are protected. If the relationship between controlled and controlling enterprises is specified in a contract, all of the agreements must be disclosed to the shareholders in both companies and reviewed by

¹⁸⁵ See *Weinberger v UOP Inc* 457 A.2d 701 (Del, 1983).

¹⁸⁶ Securities Exchange Act of 1934, Regulation S-K, Item 404(a).

¹⁸⁷ *Ibid* Item 403.

¹⁸⁸ *Ibid* Item 404(a).

¹⁸⁹ *Ibid* Item 404(b).

¹⁹⁰ NYSE's Listed Company Manual s 314.00.

¹⁹¹ *Ibid*.

¹⁹² *Aktiengesellschaft* of 2009 [Stock Corporation Act] (Germany) § 88.

¹⁹³ § 117 of the *AktG* specifies the civil liability for a person exerting his influence on the company to induce a member of the management or supervisory boards to act to the detriment of the company or its shareholders.

qualified auditors. In a *de facto* corporate group, the law requires the controlled company to make a report on the transactions it enters into with the controlling company for auditing by the external auditor and examination by the supervisory board. The power of the supervisory board to examine and approve related-party transactions is a part of its role in supervising the management. In practice, the role of the supervisory board is questionable. The literature finds that the supervisory board may not function independently. In a company with concentrated ownership, a majority shareholder dominates both the management and supervisory boards.¹⁹⁴ In a company with dispersed ownership, management generally exercises influence over the supervisory board.¹⁹⁵

Under Thai Securities Act, transactions between a company and a related person must be approved by a shareholders' meeting. A related person includes a person who directly or indirectly has control over the company, ie who has 50 per cent of the total voting rights of the company; control of the majority of votes in a shareholders' meeting; or, control over an appointment of at least half of all directors.¹⁹⁶ According to SET listing rules, such transactions must be firstly reviewed and approved by the board of directors,¹⁹⁷ then, secondly by the shareholders' meeting.¹⁹⁸ The listing rules require the company to provide the shareholders with detailed information of the transaction and of the related person. The recommendation of the board of directors must be included in the notice of the shareholders' meeting. To ensure that the interests of minority shareholders is protected, the rules require the opinion of a financial advisor, registered with the SEC, and of the company's audit committee to be attached with the notice of meeting to allow the shareholder to make an informed decision.¹⁹⁹ To approve such transaction, the approval of at least three-fourths of shareholders, excluding interested shareholders, is necessary.²⁰⁰ The exemptions to the rules are: (i) where the transactions are on ordinary commercial terms, such as the transaction in which the

¹⁹⁴ Jürgen Odenius, 'Germany's Corporate Governance Reforms: Has the System Become Flexible Enough?' (Working paper No 08/179, International Monetary Fund, 2008) 12.

¹⁹⁵ Ibid.

¹⁹⁶ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/1.

¹⁹⁷ SET Notification No Bor.Jor./Por.22-01 article 16.

¹⁹⁸ Ibid Part 2.

¹⁹⁹ Ibid article 20.

²⁰⁰ Ibid article 22.

conditions and prices are similar to other transactions made with other traders; or, (ii) with transactions with a subsidiary in which the company holds more than 90 per cent shareholding.²⁰¹ Listed companies are required to disclose to the market the details of the transaction, the names of connected persons, the scope of their interest and the opinion of the audit committee.²⁰²

Thai corporate legal practitioner saw the rights given to minority shareholders under Thai securities law and the listing rules are already too restrictive:

The listing rules strictly and clearly regulate the exercise of major shareholders' power. From my point of view, these rules are too restrictive. For example, the rules on related transactions were amended to prevent shareholders who have a related interest in the transaction from voting. In cases where major shareholders are connected to the transaction, the decision will be made by minority shareholders and minority shareholders hardly vote for such a transaction as they feel that the transaction is unfairly beneficial to majority shareholders.²⁰³

Another corporate lawyer affirmed this view but pointed out that there was a way around minority shareholders' opposition:

Companies and their management take time to prepare the projects for shareholders' approval. In many cases these projects are related transactions and as a result large shareholders cannot vote. Companies and management do not want decisions on these projects to be made by uneducated or unsophisticated shareholders. The solution for the managements is that they will persuade the sophisticated investors to vote for them. This makes sense as these projects are really beneficial to the companies and have been thoroughly considered. Letting minority shareholders decide on these issues alone is an unacceptable risk.²⁰⁴

Strict requirements in corporate and securities law and the listing rules in this area have both advantages and disadvantages. It is questionable whether leaving the decision in the hands of minority shareholders actually benefits them or the company, as related-party transactions do not always exploit the minority shareholders. They may not, as

²⁰¹ Securities and Exchange Act B.E. 2535 (Thailand) s 89/12.

²⁰² SET Notification No Bor.Jor./Por.22-01 article 16.

²⁰³ Interview with a corporate lawyer, Bangkok.

²⁰⁴ Interview with a corporate lawyer, Bangkok.

pointed out, have sufficient understanding of the importance of the transactions. In addition, as pointed out elsewhere, the controllers of family companies often wish to promote their interests of the company as a source of wealth for the next generations. The possible advantage of such a requirement is that it does require the issues to be addressed and information to be disclosed. The board of directors will pay some attention to small shareholders in order to obtain their support.²⁰⁵

In summary, the law in the three jurisdictions ensures the fairness of related-party transactions in different ways. Under Delaware law, the approval of the shareholders' meeting is required for a transaction between a company and its director. It also relies on an audit committee, shareholders' litigations, and the rules on disclosure. German law requires external auditors and the supervisory board to examine related-party transactions. Besides, there are provisions governing the transactions within a corporate group. In Thailand, the company must provide the shareholders with the opinion of an audit committee and an authorised financial advisor. To approve related-party transactions, a supermajority vote of the shareholders' meeting is required.

Thai law and listing rules on related-party transactions provide suitable protection for minority shareholders as only disinterested shareholders, generally minority shareholders, are able to approve the transactions. Relying on outsiders – an audit committee and a financial advisor – is practical as, unlike German practice, there is no internal control system existing in the Thai corporate governance system. Furthermore, unlike the US practice which encourages shareholders to bring an action, shareholders in Thai companies rarely challenge a transaction. Thai law and legal practice in shareholders' litigation is further discussed in the following chapter.

²⁰⁵ Interview with a professional independent director, Bangkok.

6.4 Conclusion

Delaware, German, and Thai laws have taken different approaches to protecting minority shareholders. These legal systems give different emphasis to the change of corporate control and the transactions between the company and the controlling shareholders. However, there are general principles that appear to be in use in all three. First of all, the details of the transactions must be disclosed to minority shareholders. Sufficient time is also allowed to minority shareholders to consider whether to approve the transactions. Secondly, a third party opinion is necessary. In the US, special committees are widely used. In Germany and Thailand the opinions of financial experts are used. Thirdly, there are special approval processes that may be difficult for a related party to control. For instance, both in the US and Thailand, related-party transactions must be reviewed by the audit committee. Thai law also prohibits interested party from voting on the transactions.

Current Thai law and listing rules are suitable for companies with concentrated ownership and weak internal control, which are the majority of listed companies. As mentioned, the conflict within concentrated ownership companies lies between controlling and minority shareholders. Thai law requires advice from outsiders such as financial advisors or an audit committee. This is suitable, as insiders – the board members – are dominated by controlling shareholders. Also, unlike German companies, there is no internal organ in Thai companies to review the transactions. Empowering disinterested experts and board members to approve related-party transactions is appropriate. The next chapter considers how the laws in three jurisdictions provide remedies to minority shareholders whose interests are damaged by the board of directors or controlling shareholders.

Chapter 7

Minority Shareholders' Remedies

- 7.1 Introduction
- 7.2 Shareholders litigations
 - 7.2.1 Derivative actions
 - 7.2.1.1 Introduction
 - 7.2.1.2 Provisions on derivative actions
 - 7.2.2 Class actions
- 7.3 The securities regulators
 - 7.3.1 The roles of securities regulators
 - 7.3.2 The roles of securities regulators: compared
 - 7.3.3 The power of the Thai SEC: reconsidered
- 7.4 Conclusion

7.1 Introduction

The previous chapters outlined and evaluated the general legal position of minority shareholders' protection in the United States, Germany, and Thailand as well as in some specific transactions. In addition to those rights and the protection provided, company law confers remedies on minority shareholders for abuse at the hands of directors and controlling shareholders. This chapter focuses on these remedies in the US, German and Thai law. Effective remedies not only compensate injured shareholders but also deter controlling shareholders and directors from exploiting a company and other shareholders. This chapter covers derivative actions, class actions, as well as the powers of securities regulators to take action to recover losses for minority shareholders. It is confined to remedies for minority shareholders who are injured by breaches of the duties of directors and controlling shareholders. It does not, therefore, deal with the remedies which have been created for general retail investors, such as remedies for breach of the periodic and continuous disclosure requirements; and misleading and deceptive statements in fundraising and takeover documents.

7.2 Shareholders litigations

Lawsuits initiated by shareholders fall into one of two categories – derivative and direct suits. Directors owe fiduciary duties to the company. The right to bring an action against the misconduct of directors therefore belongs to the company's representative and agent – the board of directors. The board may not exercise such power because of the conflicts of interest in bringing an action against itself. Shareholders instead are permitted to make a claim in the name of the company, ie a derivative action. Direct actions are brought when a shareholder's personal interests have been damaged. For instance, where the company's affairs or the resolutions of shareholders' meeting are oppressive to minority shareholders, such shareholders may seek redress for such unfair conduct. The remedies include the purchase of the shares of the minority or the winding up of the company and distributing its assets to shareholders. Such remedies, however, are rarely used by minority shareholders in listed companies because, given their small stake in the company, they do not have sufficient incentives to initiate such actions. They may be able to recover some of their losses and avoid the cost of litigation by selling their shares in a liquid market at the market price. In theory this is a fair price when it reflects the true value of the company's share.¹ Class actions are creation of the common law judiciary to permit plaintiff with a common cause of action to group their proceedings. When used by shareholders they also permit them to combine and seek remedies through a single representative. In most jurisdictions, there are now legislation and rules of court to facilitate such actions. This section discusses only the main forms of litigations – derivative and class actions, as other types of remedies are not commonly used.

7.2.1 Derivative actions

7.2.1.1 Introduction

As mentioned, derivative actions are brought against directors by shareholders on behalf of a corporation. The real injured party is the corporation as the directors owe their

¹ Robert B Thomson, 'The Shareholder's Cause of Action for Oppression' (1993) 48 *Business Lawyer* 699, 702.

duties to it.² Assets recovered are therefore returned to the pool of corporate assets. As the lawsuit benefits the corporation and all shareholders, the plaintiff shareholders are entitled to be reimbursed for the litigation costs from the company.

Encouraging minority shareholders to initiate a derivative lawsuit for director misconduct does not only benefit the corporation itself but also improves corporate governance in general by deterring potential wrongdoing.³ As any recovered assets or damages go to the corporation, they will raise the value of total assets underlying each share. In addition to compensating the company, enforcing fiduciary duties and penalising violators deters future wrongdoing.⁴ As such lawsuits enforce personal obligations and raise the risk of destroying the reputation of the directors, they can be a 'key element in reducing the agency cost inherent in the management of public companies'.⁵

Nevertheless, the efficiency and the benefits of derivative actions have been questioned. In the US, for instance, studying the relationship between derivative suits and shareholders' wealth, Fischel and Bradley found that their availability did not significantly improve shareholders' wealth.⁶ Similarly, a study by Romano showed that shareholder litigation in public companies occurred frequently and most suits were settled by agreement with minimal or no monetary remedies.⁷ There is also no clear evidence that derivative actions operate as deterrents.⁸ In addition, derivative actions may harm a corporation rather than benefit it as shareholder litigation incurs costs to the corporation and requires the board's time and effort. After dealing with time-consuming

² Tim Oliver Brandi, 'The Strike Suit: A Common Problem of the Derivative Suit and the Shareholders Class Action' (1994) 98 *Dickinson Law Review* 355, 359.

³ Ian M Ramsay and Benjamin B Saunders, 'Litigation by Shareholders and Directors: An Empirical Study of the Australian Statutory Derivative Action' (2006) 6 *Journal of Corporate Law Studies* 397, 398–9.

⁴ John C Coffee Jr and Donald E Schwartz, 'The Survival of the Derivative Suit: An Evaluation and a Proposal for Legislative Reform' (1981) 81 *Columbia Law Review* 261, 302.

⁵ Ian M Ramsay, 'Corporate Governance, Shareholder Litigation and the Prospects for a Statutory Derivative Action' (1992) 15 *University of New South Wales Law Journal* 149, 156.

⁶ Daniel R Fischel and Michael Bradley, 'The Role of Liability Rules and the Derivative Suit in Corporate Law: A Theoretical and Empirical Analysis' (1985–1986) 71 *Cornell Law Review* 261, 282.

⁷ Roberta Romano, 'The Shareholder Suit: Litigation without Foundation?' (1991) 7(1) *The Journal of Law, Economics, & Organization* 55, 84.

⁸ *Ibid.*

procedures, the action may turn out to be without merit.⁹ Morrissey claimed that, in many cases, derivative actions were initiated without the expectation of any recovery to the corporation but for the compensation to the lawyers from the settlement.¹⁰ Given these disadvantages of derivative actions, this section discusses how the law in the three jurisdictions ensures that derivative lawsuits are applied in the best interests of corporations.

7.2.1.2 Provisions on derivative actions

United States

The derivative action in the US is a mixture of borrowed English rules and the rules developed by its own judiciary.¹¹ Originally, the English derivative action was developed from group litigation.¹² The English court asserted its power to intervene in the affairs of a joint stock company as well as other collective or community activities. In doing so in a joint stock company, it paid attention to balancing the desire to prevent abuse by the majority with the recognition of self-governance within a company.¹³ US courts tended to give great weight to the right of shareholders to curb management abuse.¹⁴ As pointed out by Prunty, '[i]n comparing the cases, one cannot escape the conclusion that the British courts held a greater faith in the ability of corporations to

⁹ See Brandi, above n 2, 368–370.

¹⁰ Daniel J Morrissey, 'The Path of Corporate Law: Of Options Backdating, Derivative Suits, and the Business Judgement Rule' (2007) 86 *Oregon Law Review* 973, 996. Cf John C Coffee Jr, 'Reforming the Securities Class Action: An Essay On Deterrence and Its Implementation' (2006) 106 *Securities Class Action Reform* 1534, footnote number 5 and its accompanying text. He argued that '[t]he true "strike suit" nuisance action, filed only because it was too expensive to defend, is ... a beast like the unicorn, more discussed than directly observed'.

¹¹ For a detailed discussion on the history of derivative actions in England and the United States, see Bert S Jr Prunty, 'The Shareholders' Derivative Suits: Notes on its Origin' (1957) 37 *New York University Law Review* 980; Xiaoning Li, *A Comparative Study of Shareholders' Derivative Actions* (2007); Carol B Swanson, 'Juggling Shareholder Rights and Strike Suits in Derivative Litigation: The ALI Drops the Ball' (1992–1993) 77 *Minnesota Law Review* 1339.

¹² For further discussion, see Stephen C Yeazell, *From Medieval Group Litigation to the Modern Class Action* (Yale University Press, 1987).

¹³ Prunty, above n 11, 993.

¹⁴ Boyle observed:

[US courts] were prepared to allow the minority to sue whenever the directors refused to act in clear breach of their duty or, alternatively, whenever it could be shown that the corporation was under the control of the wrongdoer.

AJ Boyle, 'The Minority Shareholder in the Nineteenth Century: A Study in Anglo-American Legal History' (1965) 28 *The Modern Law Review* 317, 322.

govern themselves in matters not seen as affecting the public generally'.¹⁵ The first reported US derivative action case is *Taylor v Miami Exporting Co.*¹⁶ The court allowed a shareholder to sue the directors for the restoration of corporate assets taken in violation of their fiduciary duties.¹⁷ The shareholders' right was supported when the US Supreme Court affirmed the use of derivative actions in *Dodge v Woolsey*¹⁸ in which minority shareholders brought the action against outsiders.¹⁹

The Delaware General Corporation Law Section 327 specifies that only a shareholder at the time of the challenged transaction can bring a lawsuit. This ensures that the right to bring a legal action solely belongs to a shareholder injured by mismanagement.²⁰ Additionally, the plaintiff shareholder must request the board of directors, or a comparable authority, to take an action on behalf of the company before initiating his or her own action²¹ or give reasonable explanation for not making such a request.²² This is to allow the board to deal with the alleged misconduct and to restrict the courts from intervening in the internal management of the company.²³ Appropriate reasons for not making the request are not found in legislation but continued to be established by the courts.²⁴

In response to the demand made by a shareholder, a corporate board in practice usually appoints a special litigation committee composed of independent directors to decide whether it would be in the best interests of the corporation to sue. If the committee

¹⁵ Prunty, above n 11, 994.

¹⁶ *Taylor v Miami Exporting Co* 5 Ohio 162 (1831).

¹⁷ Prunty, above n 11, 988.

¹⁸ *Dodge v Woolsey* 59 US 331 (1855).

¹⁹ Prunty, above n 11, 991.

²⁰ See Robert E Sipes, 'Corporations: Stockholders' Suits: Federal Courts: Requirement of Stock Ownership at the Time of the Injury Complained of' (1939) 37(5) *Michigan Law Review* 773. The article discusses the origin of the stock ownership requirement.

²¹ In some jurisdictions, the statutory provisions require a plaintiff shareholder to make a demand on shareholders. See, eg, Rules of Civil Procedure for the Superior Courts of Arizona Rule 23.1.

²² Court Rules of the Court of Chancery of the State of Delaware Rule 23.1.

²³ Daniel R Fischel, 'The Demand and Standing Requirements in Stockholder Derivative Actions' (1976) 44(1) *The University of Chicago Law Review* 168, 171; 'Demand on Directors and Shareholders As a Prerequisite to a Derivative Suit' (1959–1960) 73 *Harvard Law Review* 746, 748–9.

²⁴ In *Aronson v Lewis*, the Delaware Court of Chancery recognised criterion that any demand would be futile:

[U]nder the [alleged] facts, a reasonable doubt is created that: (1) the directors are disinterested and independent and (2) the challenged transaction was otherwise the product of a valid exercise of business judgment.

Aronson v Lewis 473 A.2d 805 (Del, 1984) 814.

recommends the corporation not litigate, it is questionable whether the shareholder who made the demand can request the court to scrutinise the merits of the committee's recommendation. In 1979 the state and federal courts acknowledged that the decision of a special litigation committee fell within a company's business affairs and that such a judgment was therefore protected by the business judgment rule.²⁵ In other words, if the courts were satisfied that the decision was made in an informed, disinterested and diligent manner, they would not second-guess the decision.

A turning point, however, appeared in 1981 when the Supreme Court of Delaware did not follow the business judgment rule approach. In *Zapata Corp v Maldonado*,²⁶ the court established a two-part inquiry to consider a special litigation committee's recommendation. Firstly, the court would determine whether the committee made the decision independently, in good faith, with supporting reasons and based on the proof provided by the directors.²⁷ Secondly, the court would exercise its own independent business judgment in determining whether the recommendation of the special litigation committee should be approved.²⁸

Legal scholars claim that the use of a special litigation committee avoids many potential derivative actions, as special litigation committees tend not to suggest that the board initiates an action.²⁹ Dent noted that the independent directors and the board members who appointed them tended to come from similar social and economic backgrounds.³⁰ It was unlikely that the management would appoint someone who might "rock the boat".³¹ Gilson and Kraakman pointed out that 63 per cent of outside directors of public

²⁵ See *Burks v Lasker* 441 U.S. 471 (1979); *Auerbach v Bennett* 393 N.E.2d 994 (NY, 1979).

²⁶ *Zapata Corp v Maldonado* 430 A.2d 779 (Del, 1981).

²⁷ *Ibid* 788–9.

²⁸ The court noted that:

The second step is intended to thwart instances where corporate actions meet the criteria of step one, but the result does not appear to satisfy its spirit, or where corporate actions would simply prematurely terminate a stockholder grievance deserving of further consideration in the corporation's interest.

Ibid 789. The *Zapata* approach has been followed by *Kaplan v Wyatt* 499 A.2d 1184 (Del, 1985); *In re Oracle Corp Derivative Litigation* 824 A.2d 917 (Del Ch, 2003).

²⁹ See, eg, Coffee Jr and Schwartz, above n 4; Victor Brudney, 'The Independent Director – Heavenly City or Potemkin Villages?' (1982) 95 *Harvard Law Review* 597, 613.

³⁰ George W Jr Dent, 'The Power of Directors to Terminate Shareholder Litigation: The Death of the Derivative Suit' (1980–1981) 75(1) *Northwestern University Law Review* 96, 111.

³¹ *Ibid* 111–2; Joel Seligman, 'A Sheep in Wolf's Clothing: The American Law Institute Principles of Corporate Governance Project' (1987) 55 *George Washington Law Review* 325, 321–2.

companies were CEOs of other public companies.³² If a director was a member of the board in which an outside director held a position and that first director had the ability to determine the support, the outside director would receive from the boards, including reappointment, the outside director would be deferential to that director.³³ These cross-directorships clearly reduced a boards' ability to monitor other directors. Cox's research showed that special litigation committees usually viewed shareholders' request to take an action against directors as not in the best interests of the company and therefore rejected them.³⁴ From 44 cases, there was only one case in which a special litigation committee recommended pursuing the claims.³⁵

Another issue is the participation of attorneys in derivative actions. The lawyer's fees in a derivative action lawsuit in the US are normally charged on a contingent fee basis – the attorneys are paid only if the suits are successful. This practice leads to a conflict between the personal interests of the lawyers and the shareholders' interests. The plaintiff attorneys prefer speedy settlements rather than a trial as the former guarantees faster payment for their work. The latter may leave the attorneys without compensation after years of work. In settlements, the attorneys generally are a party to the negotiation process.³⁶ In some cases, the attorneys may offer a non-monetary settlement in exchange for a generous attorney fee.³⁷ The non-pecuniary relief includes the addition of independent directors to the board of directors, changes in executive compensation, and restrictions on self-interested transactions.³⁸ These may reduce future wrongdoing, however, in most cases, the changes are merely “cosmetic”. For example, in

³² Ronald J Gilson and Reinier Kraakman, 'Reinventing the Outside Director: An Agenda for Institutional Investors' (1900–1991) 43 *Stanford Law Review* 863, 875.

³³ Lisa Fairfax, 'Sarbanes-Oxley, Corporate Federalism, and the Declining Significance of Federal Reforms on State Director Independence Standards' (2005) 31 *Ohio Northern University Law Review* 381, 411–2.

³⁴ James D Cox, 'Searching for the Corporation's Voice in Derivative Suit Litigation: A Critique of *Zapata* and the ALI Project' (1982) 1982 *Duke Law Journal* 959.

³⁵ Robert B Thompson and Randall S Thomas, 'The Public and Private Faces of Derivative Suits' (2004) 57 *Vanderbilt Law Review* 1747, footnote n 147.

³⁶ See *Needham v Cruver* 1995 WL 510039 (Del Ch, 1995). The court stated:

[T]he law promotes the value of fair settlements by affording a process in which some degree of assurance can be afforded to absent class members or shareholders that the settlement is fair to them at least in the judgment of a disinterested and experienced judge.

³⁷ Edward Tsai, 'Success by another Name: Recognizing a Limited Expectation under Delaware Law to the Indemnification of Derivative Action Settlements' (2009) 64 *New York University Annual Survey of American Law* 879, 912.

³⁸ Romano, above n 7, Table 2.

approximately 50 per cent of cases in which the companies agreed to change the board members, only one or two outsiders were added to the board.³⁹ This would not bring any significant change to the corporation if the majority of the board were still controlled by insiders.⁴⁰ To ensure that the settlement is fair to all shareholders, any settlement must be approved by the court and notified to all shareholders.⁴¹ The requirement of court approval can be excluded if the dismissal is to be without prejudice or there is evidence that no compensation is directly or indirectly given to the shareholder plaintiff or his attorney.⁴²

Germany

Derivative actions in Germany are specifically created by statute rather than the procedure of the court. The right of minority shareholders to initiate claims against members of management and supervisory boards was recognised in 2005 when the *Gesetz zur Unternehmensintegrität und Modernisierung des Aktiengesetzes* of 2005 [Law on Corporate's Integrity and on the Modernization of the Stock Corporations Act] ("UMAG") was enacted.⁴³ One of the purposes of this Act is to encourage minority shareholders to sue misbehaving board members.⁴⁴ Article 148 of the *Aktiengesetz* of 2009 [Stock Corporation Act] ("AktG"), as amended by the UMAG, authorises

³⁹ Ibid.

⁴⁰ Ibid 63.

⁴¹ Court Rules of the Court of Chancery of the State of Delaware Rule 23.1. The criteria which the court applies in considering the fairness of the settlement are:

(1) the probable validity of the claims, (2) the apparent difficulties in enforcing the claims through the courts, (3) the collectibility [sic] of any judgment recovered, (4) the delay, expense and trouble of litigation, (5) the amount of the compromise as compared with the amount and collectibility [sic] of a judgment, and (6) the views of the parties involved, pro and con.

Polk v Good 507 A.2d 531 (Del, 1986) 536.

⁴² Court Rules of the Court of Chancery of the State of Delaware Rule 23.1. For a study on the roles of the courts in reviewing proposed settlements, see Carolyn Berger and Darla Pomeroy, 'Settlement Fever – How a Delaware Court Tackles its Cases' (1992–1993) 2 *Business Law Today* 7; William B Chandler, 'Awarding Counsel Fees in Class and Derivative Litigation in the Delaware Court of Chancery' (Paper presented at the Role of Judges in Corporate and Securities Law, University of Michigan Law School, 20 April 2001).

⁴³ For the historical background of the development of derivative actions in Germany, see Hans C Hirt, 'The Enforcement of Directors' Duties Pursuant to the Aktiengesetz: Present Law and Reform in Germany: Part 1' (2005) 16(4) *International Company and Commercial Law Review* 179, 184–5. Gottwald claimed that 'this is the first and only time for the minority to be empowered to enforce a claim of the total of shareholders ...'. Peter Gottwald, 'On the Extension of Collective Legal Protection in Germany' (2007) 26 *Civil Justice Quarterly* 484, 490.

⁴⁴ Jean J Du Plessis, Bernhard Grobfeld and Claus Luttermann, *German Corporate Governance in International and European Context* (2007) 60.

shareholders whose shares amount to one per cent of the share capital or a *pro rata* amount of €100,000 to claim damages caused to the company.⁴⁵ In addition to the shareholding threshold requirement, there are other prerequisites for shareholders to fulfil. The court will admit the claim from eligible shareholders if, firstly, they had acquired the shares before they became aware of the managerial misconduct.⁴⁶ Secondly, they must have requested the company to file the claim in its own name and the company failed to take action within a reasonable time.⁴⁷ Thirdly, they must present facts to support any allegation that the damages are due to dishonesty of the management or a gross breach of the law or the company's articles of association.⁴⁸ Finally, the claim will not be accepted if there are prevailing grounds in the company's interest for not bringing an action.⁴⁹ Once permission is granted, the action must be filed with the court within three months.⁵⁰ At any time, the company is empowered to assert the damages claim or to take over the pending litigation.⁵¹ In order to prevent repetitive litigation, the verdict is effective against the company and all shareholders.⁵²

To identify who will bear the litigation costs, the litigation procedure is separated into two parts: the period before the lawsuit is accepted and the period after the lawsuit is accepted. Unless the court accepts the application for consideration, the applicant must bear the costs for the first period.⁵³ However, if the court rejects the application and it appears that the company failed to communicate with the applicant before the suit was instituted, the company is obliged to reimburse such costs.⁵⁴ If the case is accepted, the company will have to bear the costs. As to the costs after acceptance, if the court's decision is wholly or partly favourable to the company, the company must reimburse the plaintiff shareholder for all the costs unless the action is brought by deliberate or gross negligence on the basis of making false allegation.⁵⁵ These provisions attempt to

⁴⁵ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 148(1).

⁴⁶ *Ibid.*

⁴⁷ *Ibid.*

⁴⁸ *Ibid.*

⁴⁹ *Ibid.*

⁵⁰ *Ibid* § 148(4).

⁵¹ *Ibid* § 148(3).

⁵² *Ibid* § 148(5).

⁵³ *Ibid* § 148(6).

⁵⁴ *Ibid.*

⁵⁵ *Ibid.*

encourage aggrieved shareholders to participate in monitoring the management while deterring shareholders from bringing meritless cases.

Another significant change has been the introduction of an electronic shareholders' forum on the digital Federal Bulletin to facilitate communication among shareholders.⁵⁶ This allows shareholders to communicate among themselves in a timely and affordable way. A shareholder may put up a notice to encourage other shareholders to collect votes or seek to help to submit a claim.⁵⁷

Although there has been an attempt to introduce derivative actions for minority shareholders in Germany, it is questionable whether this procedure is workable. To prevent unfounded or improper claims, there are criteria that shareholders must fulfil. One of the requirements permits shareholders to file a lawsuit only if it is not against the company's interests. The Federal Court of Justice provided examples of the grounds on which a court can apply to reject a petition, eg, to protect the company's reputation and to prevent negative consequences to the operations of the company.⁵⁸ Despite the examples given, the interpretation of the company's interest remains unclear. With minimal case law in Germany, the apparent unlimited scope of judicial discretion may hamper a new remedy.⁵⁹

In addition, unlike the US, contingent and conditional fee agreements with lawyers are prohibited in Germany.⁶⁰ There is also a general rule that the costs follow the event – the losing party bears its own and the winning party's litigation costs. Consequently, minority shareholders must advance the initial costs of filing the petition. Only if the court accepts the petition will the costs be reimbursed by the company. On the one hand, this can deter meritless applications. On the other hand, given their small stake in

⁵⁶ Ibid § 127a.

⁵⁷ Frank Wooldridge, 'The German UMAG of 22 September 2005' (2007) 70 *Amicus Curiae* 22, 23.

⁵⁸ Hans C Hirt, 'The Enforcement of Directors' Duties Pursuant to the *Aktiengesetz* and Reform in Germany: Part 2' (2005) 16(5) *International Company and Commercial Law Review* 216, 219.

⁵⁹ Ibid 220.

⁶⁰ Stefano M Grace, 'Strengthening Investor Confidence in Europe: US-Style Securities Class Actions and the *Acquis Communautaire*' (2006) 15(2) *Journal of Transnational Law & Policy* 281, 287. See also Danny Strassman, *Contingency Fees in Europe Examined: Germany* (2011) *Legal Finance Journal* <<http://www.legalfinancejournal.com/contingency-fees-in-europe-examined-germany/>> at 20 March 2011.

the company, it is unlikely that minority shareholders would have sufficient incentive to initiate an action. Without a direct financial incentive for them, they may see no benefit in filing such a claim. Hirt pointed out that the legislators were largely concerned with the problem of “too many actions” but failed to deal with the problem of “too few actions”.⁶¹ As indicated, the law also imposes a shareholding threshold and prerequisite requirements to filter out meritless claims. In addition, Article 149 of the *AktG* requires the company to disclose to the public the details of any discontinuance or settlement, including the details of the agreement and any payment made by the company. It is impossible for shareholders and the company to settle with a secret payment. Hirt further affirmed that the potential for derivative actions to be misused is unlikely.⁶² Without contingent fees for lawyers and incentives for minority shareholders, private enforcement actions may be infrequent in Germany.

Thailand

The concept of a derivative action in Thailand was introduced in 1911 in the Partnership and Company Act⁶³ and later codified in the Civil and Commercial Code,⁶⁴ governing private companies, but has rarely been used. Section 1169 specifies that claims against the company’s directors, for damages they cause to the company, may be brought by the company or, if the company refuses to act, by a shareholder. For public companies, Section 85 of the Public Limited Company Act of 1992 also authorises one shareholder, or shareholders holding an aggregate number of shares not less than five per cent of total shares, to bring such an action against the directors if the company fails to comply with the shareholders’ request to bring such an action. Despite the rights provided, there are some unclear issues: for example, whether the plaintiff shareholders must continually hold shares for a specific period; and, whether the plaintiff shareholders can be reimbursed all expenses relating to the action. The courts have had limited opportunities to develop this legal concept. There is no case brought to the Supreme

⁶¹ Hirt, above n 43, 223. Cf Cioffi argued that German policymakers yet failed to prevent excessive and abusive litigation. John W Cioffi, ‘Corporate Governance Reform, Regulatory Politics, and the Foundations of Finance Capitalism in the United States and Germany’ (2006) 7(6) *German Law Journal* 532, 252.

⁶² Hirt, above n 43, 222–3.

⁶³ Partnership and Company Act B.E. 2454 (1911) (Thailand) s 170.

⁶⁴ See the Thai Government Gazette Number 45, 1 January B.E. 2473 (1928) 235.

Court by shareholders in a public company.⁶⁵ Shareholders in a private company rarely initiate derivative actions and none of them discuss the above problematic issues.⁶⁶

The provision relating to derivative suits has recently been amended to encourage minority shareholders in listed companies to bring a lawsuit against mismanagement. Section 89/18 of the revised Securities and Exchange Act of 1992 (“Securities Act”) provides that shareholders may bring an action against directors for breaching their duty of care and loyalty if the shareholders collectively have not less than five per cent of the entire voting rights. Before doing so, the shareholders must demand that the company bring an action against such directors. If the company fails to proceed with the requested action within one month from the date of notice, the shareholders can bring an action on behalf of the company. The court may order the company to reimburse actual expenses to the plaintiff shareholders if the action is brought in good faith. The significant changes in the revised Securities Act are the specific period of time for a company to respond to the shareholders’ demand and the court’s power to order the company to compensate the plaintiff shareholders.

In summary, the law in the three jurisdictions allows derivative actions and attempts to prevent strike suits – actions brought without an expectation of any recovery for the corporation but for compensation from the settlement – by imposing requirements which shareholders have to fulfil. Amongst all three jurisdictions, Thai law imposes the heaviest requirements. Under Delaware law, there is no shareholding threshold requirement. This may be because of the small stake shareholders have in US companies. To meet the threshold requirement in German law, shareholders may aggregate either the required number of shares or the required value of shares. Thai law specifies only the percentage of a company’s share capital. This requirement filters out the claims brought by shareholders holding fewer shares. However, given the various

⁶⁵ Information based on the search engine provided by the Supreme Court website as of March 2012 at <http://www.deka2007.supremecourt.or.th/deka/web/search.jsp>.

⁶⁶ The significant decisions relating to derivative actions are: (i) the shareholders’ right was limited to bringing an action against the directors, not the third party (Decisions of the Supreme Court No 10878/2551; 3250/2545; 3877/2525); (ii) the plaintiff shareholders are only allowed to seek monetary compensation (Decisions of the Supreme Court No 1426/2542; 1910/2538; 4355/2536); (iii) the plaintiff shareholders are entitled to bring an action only after requesting the company to do so (Decision of the Supreme Court No 4530/2539).

sizes of Thai listed companies, it is questionable whether minority shareholders in a Thai company can possibly gather five per cent of total shares in order to bring an action. During the course of the interview conducted for this research, a former member of the Stock Exchange of Thailand pointed out that:

The law should facilitate shareholders in exercising their rights. For example, in case of a derivative suit, the law requires five per cent shareholding. In some companies with high market capitalisation, it is difficult for small shareholders to gather such an amount of the shareholding. I suggest that the law should require either the percentage of shareholding or a number of shareholders.⁶⁷

Five per cent of the average capitalisation of a company in the SET50 is approximately 6,591 million baht.⁶⁸ It is unlikely for individual Thai minority shareholders to hold shares of this value. In addition, unlike German law that provides an electronic shareholders' forum, there is no affordable and timely mechanism facilitating small shareholders' communication with each other to collect the percentage of shares required. The German approach, which employs both the number of shares and the minimal value of the share capital as the shareholding threshold, is clearly more practical. This approach considers whether the aggregated shares have sufficient value for minority shareholders to initiate an action rather than whether such a percentage of shares is significant for the company. To provide more suitable remedies for minority shareholders, Thailand should consider adopting the German approach.

An issue that has not been addressed in Thai company law is the time requirement in respect of ownership. Delaware and German laws require that the plaintiff shareholders must acquire the company's shares before they become aware of managerial misconduct. A similar rule does not exist in Thai law. Besides, Thai courts have not had an opportunity to affirm what the meaning of "shareholders" in the law implies to the shareholders at the time of knowledge of the misconduct. This requirement is significant as it can deter professional plaintiff shareholders. It is also to ensure that the plaintiff shareholders are actually affected by the alleged mismanagement. Thailand may need to consider setting this additional prerequisite.

⁶⁷ Interview with a former member of the Stock Exchange of Thailand, Bangkok.

⁶⁸ The capitalisation of the SET50 is 6,591,087.41 million baht. *Market Statistics* (2012) The Stock Exchange of Thailand <http://www.set.or.th/en/market/market_statistics.html> at 20 March 2012.

Thailand has adopted derivative actions since 1911. However, it is questionable whether the adopted rule can effectively function in the Thai context. As mentioned above, no derivative action relating to a public company has been brought to the Supreme Court. This is mainly because under the previous version of the Public Limited Company Act minority shareholders had to bear the cost of litigation. The amendment in 2008 in the Securities Act encourages minority shareholders to bring such a claim by requiring the company to reimburse the litigation costs to the plaintiff shareholders if the action is brought in good faith.⁶⁹ Despite this, the minority shareholders may still be reluctant to initiate a lawsuit. Even if a plaintiff shareholder wins the case, he or she does not receive any direct financial benefit. There are also some problems in practice. A Thai corporate lawyer confirmed this, saying:

Theoretically, I see derivative actions benefiting minority shareholders. In the past, shareholders had no incentive to bring the case to the court as they themselves had to bear litigation cost. They also did not want to spend time. Though the new Securities Act specifies that companies must compensate for all costs incurred by the shareholders in relation the lawsuit, in practice no shareholder wants to spend time for the lawsuit considering their small numbers of shares and no direct financial benefit to them.⁷⁰

A Thai public prosecutor agreed and pointed to other factors:

Minority shareholders hardly exercise their legal rights. Partly, it is because most investors are speculators, rather than long-term investors. They do not care about firm performance and financial reports. Even if there is a fraud, they have no interest in bringing an action against wrongdoers. Another significant point is the difficulties in predicting the outcome of the case as there is no precedent which they can rely on. Besides, the evidence for proving liability is usually with the accused. Though the shareholders can access the company documents, it is uncertain whether they will obtain the information which can prove liability.⁷¹

In addition, although the court is empowered to reimburse the litigation costs to plaintiff shareholders, in practice, they may still have to personally bear some of the litigation fees. Under Thai civil procedure law, similar to the German approach, if the verdict is

⁶⁹ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 89/18.

⁷⁰ Interview with a corporate lawyer, Bangkok.

⁷¹ Interviews with a public prosecutor, Bangkok.

unfavourable to the plaintiff, the plaintiff is generally liable to the defendant for the latter's legal fees.⁷² The court may order the losing directors to compensate the prevailing shareholders for the shareholders' legal fees, which are calculated from the damages claimed, not the amount recovered. According to the Civil Procedural Code, the total attorney's fees which the court may order the losing party to compensate must not exceed five per cent of the damages claimed in the court of first instance,⁷³ and three per cent of the damages claimed in the Court of Appeal and the Supreme Court.⁷⁴ This is much lower than the actual attorney's fees.⁷⁵ It is therefore likely that the plaintiff shareholders will have to personally pay the attorney's fees in excess of this amount.

The other factor that makes derivative actions in Thailand rare is the limited role of Thai lawyers. In Thailand, contingent and conditional fees are prohibited. The Thai Supreme Court views such arrangements as contrary to the public interest.⁷⁶ Thus the role played by Thai attorneys is different from that of US ones. The fee awarded to the US attorneys generally depends on the outcome of the suit; therefore, they become the like parties with an interest in the case.⁷⁷ They bring the case to the public's attention, initiate it, and even negotiate its settlement. On other hand, Thai lawyers cannot initiate the case and, although permitted to, take a very limited part in negotiating. Regardless of the outcome, Thai attorneys will eventually earn their fees either from the plaintiff or the defendant. The decision to bring or not to bring an action therefore solely belongs to the shareholders.

In the US, a negative consequence of the contingency fee arrangement has been the large number of settlements for the benefit of lawyers. This issue may not be a problem in Thailand. Under US common law, if the case is settled, the company must reimburse

⁷² Civil Procedure Code B.E. 2477 (1934) (Thailand) s 161.

⁷³ Ibid schedule 6.

⁷⁴ Ibid.

⁷⁵ Central Intellectual Property and International Trade Court Thailand, 'The Judicial System in Thailand: An Outlook for a New Century' (IDE Asian Law Series No 6, Institute of Developing Economies, 2001) 109.

⁷⁶ Decision of the Supreme Court No 6919/2544. The court held that the agreement to have the attorney's fee at a percentage of the plaintiff's recovery if the action is successfully litigated was against public policy. Such agreement was therefore void under the Civil and Commercial Code s 150.

⁷⁷ Coffee Jr and Schwartz, above n 4, 309.

the reasonable litigation fees and expenses of both parties.⁷⁸ The plaintiff shareholders' attorneys in the US prefer speedy settlements to trials because the former ensures that their work will be compensated.⁷⁹ The plaintiff shareholders are therefore only "figurehead" plaintiffs.⁸⁰ On the other hand, under the Thai legal system, the settlement is made between the defendant directors and the plaintiff shareholders who have a direct interest in the company, not the attorneys. It is unlikely that the case can be settled. Given these different approaches, the concern with attorneys' conflicts of interest in settlements leading to cosmetic settlements and to obtain fees is unlikely to be a problem in Thailand.

In summary, the concept of derivative actions has been long incorporated into the Thai legal system but their adoption has not brought, and will not produce, similar consequences as in the US. Without contingent fees, cases brought by minority shareholders in Thailand are likely to continue to be minimal. On the one hand, Thailand has not encountered massive strike suits or cosmetic settlements. On the other hand, given the limited number of actions, private enforcement of the law has played almost no role in deterring mismanagement or in recovering corporate loss. This suggests that Thailand should consider both encouraging minority shareholders to initiate actions and deterring professional plaintiff shareholders. From the German experience, Thailand may adopt the requirement on the nominal value of shares to make the shareholding requirement practical for all sizes of companies. In addition, setting up an electronic forum is an affordable and practical method to allow minority shareholders to share their concerns and aggregate their shares and votes. To filter out professional plaintiff shareholders, Thailand should adopt a requirement to ensure that plaintiff shareholders have been truly damaged by any managerial misconduct.

⁷⁸ John C Coffee Jr, 'The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation' (1985) 48(3) *Duke University School of Law* 5, 16–17.

⁷⁹ Ibid 17.

⁸⁰ See Kenneth E Scott, 'Corporation Law and the American Law Institute Corporate Governance Project' (1983) 35(5) *Stanford Law Review* 927, 940; Jeffrey Bauman, Elliott Weiss and Alan Palmiter, *Corporations Law and Policy: Materials and Problems* (5th ed, 2003) 960.

7.2.2 Class actions

In the US, the other type of shareholders' litigation that has become common in the last 20 years is a class action. This action allows a large number of shareholders, each of whom often holds small fractions of shares, to cost-efficiently aggregate their claims against a corporation.⁸¹ Without this mechanism, each of those shareholders would be unlikely to bring an action as their stakes are too small to justify the time, effort and expense of a lawsuit. The rise of direct claims began in 1990 when the share market boomed with a large number of initial public offerings of securities made by high-tech companies.⁸² As a result, a lot of people were attracted to investment without understanding the risk of business. When the share prices substantially dropped, these investors assumed that there was fraud and brought class actions.⁸³ It is claimed that investors who had understood the investment in such a high-risk business also joined in the actions as "free riders with nothing to lose".⁸⁴ The critical factor driving the growth of class actions was contingent fee arrangements. Similar to derivative actions, attorneys who represented a large group of shareholders had a direct interest in the action as they initiated the case, brought an action, and even settled the suit.⁸⁵ It is claimed that attorneys were willing to file lawsuits even in non-meritorious cases if they could get some reward. A securities class action became a weapon to threaten companies rather than a mechanism to recover minority shareholders' damages.⁸⁶ The corporate lobby also complained that its members were harassed by frivolous class action.⁸⁷ Although a number of observers pointed out abuses in private litigation, there

⁸¹ See, eg, Alexandra Lahav, 'Fundamental Principles for Class Action Governance' (2003) 37(1) *Indiana Law Review* 65.

⁸² Arthur R Pinto and Douglas M Branson, *Understanding Corporate Law* (2nd ed, 2004) 479.

⁸³ *Ibid.*

⁸⁴ Steven Sharpe and James Reid, 'Aspects of Class Action Securities Litigation in the United States' (1997) 28(3) *Canadian Business Law Journal* 348, 354.

⁸⁵ For a discussion on the roles of attorneys in class actions, see Barbara Warnick Thompson, 'Attorneys' Fees in Class Action Shareholder Derivative Suits' (1984) 9(3) *Delaware Journal of Corporate Law* 671; Nancy J Moore, 'Who Should Regulate Class Action Lawyers' (2003) 2003(5) *University of Illinois Law Review* 1477; Bruce H Kobayashi and Larry E Ribstein, 'Class Action Lawyers as Lawmakers' (2004) 46(4) *Arizona Law Review* 766.

⁸⁶ Leslie Brueckner and Arthur H Bryant, 'Fighting to Stop Class Action Abuse' (2001–2002) 4 *TortSource* 3.

⁸⁷ David M Levine and Adam C Pritchard, 'The Securities Litigation Uniform Standards Act of 1998: The Sun Sets on California's Blue Sky Laws' (1998) 54 *Business Lawyer* 1, 1–2.

was no statistical evidence supporting a class action crisis.⁸⁸ Despite the lack of evidence, the Congress enacted the Private Securities Litigation Reform Act of 1995,⁸⁹ which required shareholders who wished to initiate lawsuits with the Federal Court to clearly state a deliberate fraud.⁹⁰ The Act also dealt with the problems of professional plaintiffs, inadequate disclosure of the terms of settlements, and excessive attorney's fees. To circumvent this Act, shareholders' attorneys, where possible, filed in state courts instead of the Federal Court.⁹¹ These practices, however, were later prohibited when the Securities Litigation Uniform Standards Act of 1998 was enacted.⁹²

The factor that currently spurs the growth of class actions in the US is litigation funding.⁹³ Litigation financing is the 'practice of providing money to a party to pursue a potential or filed lawsuit in return for a share of any damages award or settlement'.⁹⁴ This approach has received much attention as it allows a third party to the attorney-client relationship although he or she has no interest in justice and, unlike lawyers, owes no fiduciary duties to the plaintiff.⁹⁵ The legal status of litigation financing remains unclear. No states prohibit litigation financing and only three states regulate it – Maine, Nebraska and Ohio.⁹⁶ However, no court has clearly ruled on the validity of third party litigation agreements.⁹⁷ Third party litigation financing is controversial. On the one hand, it could increase frivolous litigation and raise ethical concerns. On the other hand, given high litigation costs, this approach provides a chance to those who cannot afford

⁸⁸ John W Avery, 'Securities Litigation Reform: The Long and Winding Road to the Private Securities Litigation Reform Act of 1995' (1996) 51 *Business Lawyer* 335, 339–341.

⁸⁹ For details of the Reform Act, see Jill E Fisch, 'Class Action Reform: Lessons from Securities Litigation' (1997) 41(2) *Arizona Law Review* 533.

⁹⁰ 15 USC § 78u-4(b)(1).

⁹¹ Mukesh Bajaj, Sumon C Mazumdar and Atulya Sarin, 'Securities Class Action Settlements' (2003) 43(3) *Santa Clara Law Review* 1001, 1005–6.

⁹² *Ibid* 1006.

⁹³ For general discussion of litigation financing, see Paul Bond, 'Making Champerty Work: An Invitation to State Action' (2001–2002) 150 *University of Pennsylvania Law Review* 1297 (including an appendix of state laws); Susan Lorde Martin, 'Litigation Financing: Another Subprime Industry that has a Place in the United States Market' (2008) 53 *Villanova Law Review* 83.

⁹⁴ John Beisner, Jessica Miller and Gary Rubin, *Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States* (2009) the US Chamber Institute for Legal Reform <<http://www.instituteforlegalreform.com/images/stories/documents/pdf/research/thirdparty litigation financing.pdf>> at 20 March 2012, 1.

⁹⁵ *Ibid* 2.

⁹⁶ Jason Lyon, 'Revolution in Progress: Third-Party Funding of American Litigation' (2010) 58 *UCLA Law Review* 571, 575.

⁹⁷ *Ibid* 575–6.

to assert a claim. Given its benefits, a number of scholars suggest regulating this approach rather than prohibiting it.⁹⁸

Litigation funding also currently attracts public attention, as it becomes a part of the investment market.⁹⁹ A number of litigation funding companies offer third party litigation financing across the world.¹⁰⁰ And, furthermore, hedge funds have started to invest in litigation.¹⁰¹ The entrance of litigation funders into the US obviously increases the number of class actions. The question of how the US will deal with this situation and whether it will allow this approach like other common law jurisdiction – Australia and England – will be interesting for Thailand to learn from.

In Germany, there is a model case procedure to be used in capital market mass litigation which is different from US class action. To initiate a lawsuit, under the *Kapitalanleger-Musterverfahrensgesetz* of 2005 [Capital Market Model Case Act] (“*KapMuG*”), a plaintiff shareholder must submit an application for the establishment of a model case to the Appellate Court (*Oberlandesgericht*).¹⁰² Such an application must contain all the facts, points of dispute, as well as sufficient evidence.¹⁰³ If the application is accepted, the court will announce this in the electronic Federal Gazette.¹⁰⁴ Within four months from that announcement, if at least another nine shareholders submit applications to the Appellate Court on the same subject matter, the court will refer the case to the Higher Regional Court.¹⁰⁵ Once the model case proceeding is referred to the Higher Regional Court, all pending applications submitted to the court trying the matter will be suspended.¹⁰⁶ The model case ruling delivered by the Higher Regional Court is binding on the Appellate Court in respect of the same matter.¹⁰⁷ The Appellate Court then

⁹⁸ Susan Lorde Martin, 'The Litigation Financing Industry: The Wild West of Finance Should be Tamed Not Outlawed' (2004–2005) 10 *Fordham Journal of Corporate & Financial Law* 55; Julia H McLaughlin, 'Litigation Funding: Charting a Legal and Ethical Course' (2006–2007) 31 *Vermont Law Review* 615; Lyon, above n 96.

⁹⁹ Deborah Hensler, 'The Future of Mass Litigation: Global Class Actions and Third-Party Litigation Funding' (2011) 79(2) *George Washington Law Review* 306, 320–2.

¹⁰⁰ Such as Allianz Prozess Finanz (Germany), IM Litigation Funding (UK), and IMF (Australia).

¹⁰¹ See Larry E Ribstein, 'The Death of Big Law' (2010) 2010 *Wisconsin Law Review* 749, 801–2.

¹⁰² *Kapitalanleger-Musterverfahrensgesetz* of 2005 [Capital Market Model Case Act] (Germany) § 1(1).

¹⁰³ *Ibid* § 1(2).

¹⁰⁴ *Ibid* § 2(1).

¹⁰⁵ *Ibid* § 4(1).

¹⁰⁶ *Ibid* § 7.

¹⁰⁷ *Ibid* §14(1).

decides all the pending proceedings on the basis of the model case ruling.¹⁰⁸ Unlike US class actions, the German model encourages individual shareholders to initiate proceedings themselves.¹⁰⁹ A critical point is the law does not impose a shareholding requirement so that one minor shareholder can initiate an action. The electronic Federal Gazette permits other shareholders to check whether there are any pending proceedings relating to their shares. The *KapMuG* was to lapse on 1 November 2010. This limited period allowed the legislators to evaluate its effectiveness and decide to extend the Act or amend the details of its procedures. The Act was extended for two years but its efficiency or inefficiency remains unclear.¹¹⁰

In Thailand, there is no procedure similar to US securities class actions or the *KapMuG*. However, under Thai Civil Procedure law, shareholders may jointly file a lawsuit as co-plaintiffs, or after a case has been brought by a shareholder, other shareholders can submit requests to the court to join the case.¹¹¹ There is a significant number of issues to take into account in considering whether to adopt schemes like those of the US and Germany to Thailand. One is whether Thailand should adopt the US or German class action procedures or establish its own model which is more suitable to the local context. If the US approach was to be selected, there is the critical question of how to prevent the abuse of actions. The key in the difficulty of adopting this legal concept is firstly how to fit a class action into Thai procedural law. Under Thai procedural law, group litigation is not recognised. The third parties can join a lawsuit as co-plaintiffs or interpleaders. Given the specific character of class actions, procedural law that applies to other civil cases cannot be employed with class actions. Secondly, minority shareholders may be reluctant to initiate a lawsuit. As indicated, contingent fee arrangements are not allowed

¹⁰⁸ Ibid § 14(2).

¹⁰⁹ The German "Capital Markets Model Case Act" (2010) Bundesministerium der Justiz <http://www.bmj.de/SharedDocs/Downloads/DE/pdfs/KapMuG_english.pdf> at 20 March 2012, 2.

¹¹⁰ Rhonda Wasserman, 'Transnational Class Actions and Interjurisdictional Preclusion' (2011) 86 *Notre Dame Law Review* 313, 365. Hilgard and Kraayvanger claimed that the *KapMuG* was not suitable for a case with a large number of claimants. Mark Hilgard and Jan Kraayvanger, 'Class Actions and Mass Actions in Germany' (2007) September 40 <http://www.mayerbrown.com/public_docs/Class_Actions_Mass_Actions_Germany.pdf> at 20 March 2012. Feess and Halfmeier argued that the Act led to higher costs and discouraged small shareholders from litigation. Eberhard Feess and Axel Halfmeier, *The German Capital Markets Model Case Act (KapMuG) – A European Role Model For Increasing the Efficiency of Capital Markets? Analysis and Suggestions for Reform* (2010) Social Science Research Network <<http://ssrn.com/abstract=1684528>> at 20 March 2012.

¹¹¹ See Civil Procedural Code as amended (No 18) B.E. 2551 (2008) (Thailand) s 57–9.

in Thailand. Minority shareholders have to advance all litigation and legal costs. Besides, they may see that the benefit from the litigation is not worth the time and effort which may extend over years. Given the different backgrounds of US and Thai law, Thailand may consider an alternative model,¹¹² the German approach, which relies on the decision of the higher court. All of the interviewees acknowledged that a class action is a better alternative for minority shareholders in taking legal action.¹¹³ One interviewee expressed his concerns about the use of class actions:

Regarding class actions, the significant advantage is that it grants the means to injured shareholders to recover their loss. However, it is necessary to consider its side effect on the management. Dishonest minority shareholders can employ the action to interrupt companies' business. If we decide to allow minority shareholders to bring a class action, the law should impose some measure to prevent its misuse.¹¹⁴

7.3 The securities regulators

In addition to private actions, minority shareholders may be protected by public agencies enforcing the law – securities regulators. The role of supervisory agents is critically important to market development. Public enforcement ensures regulatory compliance, improves investor protection, and provides long-term benefits to the market. In addition, public enforcement can complement private actions to compensate injured shareholders and deter wrongdoers. The key question is to what extent the securities supervisors should exercise their authority to protect, and reimburse, minority shareholders. This section seeks, firstly, to provide the background of securities regulators in the three jurisdictions; secondly, to compare and explain the differences among the authorities of the three securities regulators; and finally, to discuss how to improve the role of the Thai securities regulator.

¹¹² For details of the concept of functional convergence, see John C Coffee Jr, 'The Future as History: The Prospects for Global Convergence in Corporate Governance and its Implications' (1999) 93 *Northwestern University Law Review* 641; Micheal S Gibson, 'Is Corporate Governance Ineffective in Emerging Markets?' (Working Paper No 99-63, Federal Reserve Board FEDS, 2002).

¹¹³ Interviews with professional independent directors, corporate lawyers, a public prosecutor, a judge, the officers of the SEC, the officer of the SET, and academic researchers, Bangkok.

¹¹⁴ Interview with a corporate lawyer, Bangkok.

7.3.1 The roles of securities regulators

United States

In the US, the core organisation supervising the securities market is the Securities and Exchange Commission (“SEC”). The SEC was established after the Wall Street crash in 1929. The crash greatly impacted the US economy and resulted in a massive global economic depression. The failure was caused by stock market malpractice including price manipulation, insider trading, and spreading misinformation. This led to a series of legislative reforms in the US capital markets including the Securities Act of 1933, the Securities Exchange Act of 1934, and the Banking Act of 1935. The SEC was founded by Section 4(a) of the Securities Exchange Act of 1934 (“Exchange Act”) to oversee trading on stock exchanges and ensure compliance with securities laws. During the 1950s, when the US stock markets grew substantially, the SEC became inactive and its budget was heavily cut.¹¹⁵ Also, the role of the SEC was limited to detecting and preventing or penalising violations.¹¹⁶ Its function did not include compensating injured individuals. However, the SEC’s role in redressing injured shareholders changed dramatically in 1990. With the enactment of the Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (“Remedies Act”), the SEC was authorised to order disgorgement from wrongdoers and distribute the compensation to investors.¹¹⁷ The main purpose of disgorgement was to deter wrongdoing, not reimburse injured investors.¹¹⁸ Later, after the collapse of the giant corporations, including Enron and WorldCom, which caused shareholders to lose billions, the Congress responded by enacting the Sarbanes-Oxley Act of 2002 (“SOX Act”). Under the SOX Act, the authority of the SEC extends to seeking compensation for harmed investors.

The Securities Act of 1934 granted the SEC a very broad authority to prevent legal violations. Firstly, the SEC is empowered to investigate and initiate an action for an

¹¹⁵ Henry Laurence, 'Spawning the SEC' (1998–1999) 6 *Indiana Journal of Global Legal Studies* 647, 659.

¹¹⁶ Verity Winship, 'Fair Funds and the SEC's Compensation of Injured Investors' (2008) 60 *Florida Law Review* 1103, 1110–11.

¹¹⁷ See, eg, *Ibid* 1117–8.

¹¹⁸ *Ibid* 1117; Barbara Black, 'Should the SEC Be a Collection Agency for Defrauded Investors?' (2007–2008) 63 *Business Lawyer* 317, 321.

injunction to the court when the SEC finds that any person is engaged, or is about to be engaged, in violation of the securities laws.¹¹⁹ In addition to an injunction, the court may prohibit such persons from acting as an officer or director.¹²⁰ Secondly, if the offenders are brokers or dealers, the SEC could initiate an administrative action to limit the activities of such brokers or dealers for a period not exceeding 12 months.¹²¹ Thirdly, the SEC is empowered to make administrative cease-and-desist orders. If the SEC finds that any person is violating, has violated, or is about to violate any provisions of securities laws, it may order such person to cease and desist from committing such violation and any future violation. Contrary to the injunctive action, cease-and-desist legal orders do not require the SEC to show a likelihood of a future violation.¹²² Besides, the SEC can proceed with the order in its own forum or in the court.¹²³ This legal tool is to allow the SEC full power to prevent future violations.

In addition to preventive measures, the SEC is empowered to take court action for civil monetary penalties against wrongdoers. Originally, the Exchange Act did not give the SEC the power to fine wrongdoers. In 1984, the Insider Trading Sanctions Act granted such power to the SEC in relation to inside trading cases. Later, the Congress, in the Remedies Act of 1990, decided to expand the SEC's authority to other areas of securities laws as it viewed the disgorgement remedy as an effective deterrence to violation.¹²⁴ As amended by the Remedies Act, the Exchange Act enabled the SEC to seek monetary penalties against wrongdoers by bringing an action.¹²⁵ Three levels of penalty were ordered based on the severity of the action or omission.¹²⁶ The monetary penalties must be paid to the US Treasury, not the injured parties.¹²⁷ Similarly, in administrative proceedings, the SEC is authorised to determine monetary penalties

¹¹⁹ Securities Exchange Act of 1934 § 21(d)(1).

¹²⁰ Ibid § 21(d)(2).

¹²¹ Ibid § 15(b)(4).

¹²² Louis Loss and Joel Seligman, *Fundamental of Securities Regulation* (2004) 1509.

¹²³ Securities Act of 1933 § 8A.

¹²⁴ As mentioned as one of the purposes of the Remedies Act:

The legislation addresses the disturbing levels of financial fraud, stock manipulation and other illegal activity in the US markets by authorizing new civil money penalties to deter unlawful conduct by increasing the financial consequences of securities law violations.

Senate Report No 101-645, 101st Congress, 2d Session (1990) 5451.

¹²⁵ The Securities Exchange Act of 1934 § 21(d)(3)(A).

¹²⁶ Ibid § 21(d)(3)(B).

¹²⁷ Ibid § 21(d)(3)(C)(i).

against offending brokers, dealers and analysts¹²⁸ if the penalties are in the public interest.¹²⁹ The same three levels of penalty are applied.¹³⁰ In addition to monetary penalties, the SEC can issue a disgorgement order.¹³¹ This is to ensure that ‘respondents in administrative proceedings do not retain ill-gotten gains’.¹³²

Originally, the core function of the SEC did not include collecting funds to compensate investors. A Senate Report in 1990 stated:

In contrast to damages granted in private actions, which are designed to compensate the victims of a violation, disgorgement forces a defendant to give up the amount by which he was unjustly enriched.¹³³

In practice, however, the SEC might have the discretion to ask the court to distribute disgorged funds to injured investors.¹³⁴ When such distributions were not economically feasible, the SEC asked the court to directly transfer the disgorged funds to the Treasury.¹³⁵ In 2002 SOX Act explicitly authorised the SEC to collect funds to reimburse injured investors. The Fair Fund provision states that when the SEC requests a disgorgement or a civil penalty order, it may include a civil penalty to be paid to the injured investors as part of a disgorgement fund.¹³⁶ As the statute provides the SEC with a broad authority to decide whether to distribute penalties to compensate investors,¹³⁷ the SEC announced that, based on economic feasibility, the Fair Fund would be distributed whenever possible and paid directly to the Treasury only when the compensation was too small to be distributed to a large number of injured investors.¹³⁸

¹²⁸ Ibid § 21B(a).

¹²⁹ Ibid § 21B(c).

¹³⁰ Ibid § 21B(b).

¹³¹ Ibid § 21B(e).

¹³² Senate Report No 101-645, 101st Congress 2nd Session (1990) 5466. Black found that in the mid-2000s the SEC applied the disgorgement remedy in two circumstances, namely: (i) when a corporate insider profited from the changing price of the corporation’s securities as a result of misinformation; and (ii) when an entity disclosed misleading information in connection with sales of securities, such as the Ponzi scheme. Black, above n 118, 321–2.

¹³³ Senate Report No 101-645, 101st Congress 2nd Session (1990) 5466.

¹³⁴ Winship, above n 116, 1112–3.

¹³⁵ Ibid 113.

¹³⁶ The Sarbanes-Oxley Act of 2002 § 308(a).

¹³⁷ The Fair Fund provision states:

[T]he Commission also obtains pursuant to such laws a civil penalty against such person, the amount of such civil penalty *shall, on the motion or at the direction of the Commission*, be added to and become part of the disgorgement fund for the benefit of the victims of such violation. (Italic added)

¹³⁸ Winship, above n 116, 1119–20.

The SEC is heavily criticised for its ineffectiveness in enforcement and, more recently, on its inability to compensate injured investors. Many researchers point out that the SEC is charged with varied responsibilities concerning the overall operation of the market; however, its role in preventing major frauds is clearly unsuccessful. As stated by Katz, the former Secretary of the SEC for 20 years:

In fact, for each of the scandals of the recent past one may find an analogous scandal from an earlier time. Before the [Nasdaq] market makers and [New York Stock Exchange] specialists, there was the Re and Re Scandal in the late 1950s. Before Bernard Madoff there was Bernard Cornfield. Before Enron and Worldcom there was Equity Funding. Before the SEC failed to listen to Harry Markopolous, they failed to listen to Ray Dirks.¹³⁹

In addition to a series of failures to detect major wrongdoings in Wall Street, the critics argue that the agency lacks ‘the capacity to understand operation of the securities markets’;¹⁴⁰ that the enforcement division and its implemented policy are dysfunctional;¹⁴¹ and that the SEC should be abolished and the SEC’s essential functions should be transferred to the executive branches, such as the Treasury Department and the Justice Department.¹⁴² A number of scholars and commentators also question whether the SEC should act as a collecting agency for injured investors. Given its limited resources, its duties to not only deter fraud but also collect civil damages far exceed its capacity.¹⁴³ Black affirmed that, despite the strike suits, private actions – class actions – were ‘the most effective mechanism for shareholder compensation’.¹⁴⁴ Winship also concluded that ‘the SEC is unlikely to be able to take over the compensatory role from private litigations’.¹⁴⁵

¹³⁹ Jonathan G Katz, 'Reviewing the SEC, Reinvigorating the SEC' (2009–2010) 71 *University of Pittsburgh Law Review* 489, 489–50.

¹⁴⁰ Walter Werner, 'The SEC as a Market Regulator' (1984) 70 *Virginia Law Review* 755, 784. Similarly Langevoort suggested that the SEC was outdated. Donald C Langevoort, 'The SEC, Retail Investors, and the Institutionalization of the Securities Markets' (2009) 95 *Virginia Law Review* 1025, 1025–6.

¹⁴¹ Renee M Jones, 'Will the SEC Survive Financial Regulatory Reform?' (2009–2010) 71 *University of Pittsburgh Law Review* 609, 616–7; See, James D Cox, Randall S Thomas and Dana Kiku, 'SEC Enforcement Heuristics: An Empirical Inquiry' (2003–2004) 53 *Duke Law Journal* 737, 757–60. The article pointed out the limitation on the SEC’s funding and its staff.

¹⁴² AC Pritchard, 'The SEC at 70: Time for Retirement?' (2004–2005) 80 *Notre Dame Law Review* 1073, 1101–2.

¹⁴³ Adam Reiser, 'Compensating Defrauded Investors While Preserving the SEC's Mission of Deterrence: A Call for Congress to Counteract the Troubling Consequences of Stoneridge' (2009) 2009 *Utah Law Review* 257, 263–4.

¹⁴⁴ Black, above n 118, 346. See also Cox, Thomas and Kiku, above n 141.

¹⁴⁵ Winship, above n 116, 1131.

Now the SEC is again criticised for failing to notice and prevent the current financial crisis. A large number of investors invested in asset-backed securitisation relying on the reports made by credit rating agency companies. However, the SEC did not ensure the quality and accuracy of their ratings.¹⁴⁶ The Federal Reserve also did not supervise large investment banks when they engaged in inordinate risk, such as nonprime mortgage securitisation and require them to hold adequate capital and liquidity for their activities.¹⁴⁷

The role of the SEC has been significantly readdressed in the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), which came into effect in July 2010 in response to calls for reform in securities regulation. The Act is considered as ‘the most comprehensive financial regulatory overhaul since the Great Depression’.¹⁴⁸ The purpose of the Act is:

To promote the financial stability ... by improving accountability and transparency in the financial system, to end “too big to fail”, to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices ...¹⁴⁹

The Dodd-Frank Act provides the SEC with more funding, more power to gather information, and more power to regain public confidence in the financial system in preventing another financial crisis.¹⁵⁰ These increases are supposed to improve the SEC’s ability to keep pace with market growth and technical changes. The impact of the reform will not be known for some time as it will take years for the SEC to implement the new rules and its recently located authorities.

¹⁴⁶ The Financial Crisis Inquiry Commission, *The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States* (2011) 126.

¹⁴⁷ Ibid 155, 297.

¹⁴⁸ Ross Colvin, ‘Obama Signs Sweeping Wall Street Overhaul into Law’, *Reuters* (Washington), 21 July 2010 <<http://www.reuters.com/article/2010/07/22/us-financial-regulation-obama-idUSTRE66K1QR20100722>> at 20 March 2012.

¹⁴⁹ Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

¹⁵⁰ For instance, in administrative cease-and-desist proceedings, originally, only the Federal Court could award additional amounts as a penalty to deter future misconduct. The Dodd-Frank Act allows the SEC to impose the penalty in administrative proceedings. Dodd-Frank Act § 929P. Regarding the budget, the Act doubles the SEC’s budget and also establishes the SEC ‘Reserve Fund’ which is replenished in US\$50 million annual increments out of the fees collected by the SEC. Dodd-Frank Act § 991.

Germany

In Germany, the market supervisor was established in the 1990s under a government policy of developing a sustainable capital market. In 1994 the German legislature passed the Second Financial Market Promotion Act with the intention of adopting international standards in the German securities market and to implement the requirements of European Community Directives.¹⁵¹ One of the core elements of the Second Financial Market Promotion Act was to establish the new *Bundesaufsichtsamt für den Wertpapierhandel* [Federal Securities Supervisory Office] (BAWe). The BAWe was governed by the *Wertpapierhandelsgesetz* [Securities Trading Act] (“*WpHG*”). Its functions were to supervise securities trading and ensure the integrity as well as transparency of the German market.¹⁵² In 2002 the German government passed the *Gesetz über die integrierte Finanzaufsicht* [Financial Services and Integration Act], which merged three supervisory agencies¹⁵³ into one financial regulator called *Bundesanstalt für Finanzdienstleistungsaufsicht* [Federal Financial Supervisory Authority] (“BaFin”).¹⁵⁴ The authorities and responsibilities of BaFin cover various areas under different laws. In securities market supervision, the BaFin is empowered by the *WpHG* to ensure the orderly conduct of trading¹⁵⁵ and monitor legal compliance.¹⁵⁶ To fulfil these responsibilities, the statute empowers the BaFin to issue appropriate and necessary orders for its enforcement,¹⁵⁷ request detailed information from related persons,¹⁵⁸ and audit the investment services enterprises.¹⁵⁹ The *WpHG* also requires all securities trading enterprises to notify the BaFin of any necessary facts to facilitate the BaFin in detecting any suspicious transactions, such as insider trading and market

¹⁵¹ Laurence, above n 115, 680.

¹⁵² Norbert Horn, *German Banking Law and Practice in International Perspective* (1999) 306; *Functions & history* (2012) Bundesanstalt für Finanzdienstleistungsaufsicht <http://www.bafin.de/EN/BaFin/FunctionsHistory/functionshistory_node.html> at 20 March 2012.

¹⁵³ *Bundesaufsichtsamt für den Wertpapierhandel* [Federal Securities Supervisory Office], *Bundesaufsichtsamt für das Kreditwesen* [Federal Banking Supervisory Office], and *Bundesaufsichtsamt für das Versicherungswesen* [Federal Insurance Supervisory Office].

¹⁵⁴ For details on the discussion of BaFin, see Kenneth K Mwenda, 'Legal Aspects of United Financial Services Supervision in Germany' (2003) 4(10) *German Law Journal* 1009.

¹⁵⁵ *Wertpapierhandelsgesetz* of 1998 [Securities Trading Act] (Germany) § 4(1).

¹⁵⁶ *Ibid* § 4(2).

¹⁵⁷ *Ibid* § 4(2).

¹⁵⁸ *Ibid* § 4(3).

¹⁵⁹ *Ibid* § 35(1).

manipulation.¹⁶⁰ In addition to the BaFin, each of the eight stock exchanges in Germany is also regulated by an independent agency under *Börsengesetz* [Stock Exchange Act].¹⁶¹

If the BaFin's investigation reveals a certain violation of the securities laws, for example, market manipulation,¹⁶² directors' dealing without disclosure,¹⁶³ and failure to report changes in the percentage of voting rights,¹⁶⁴ it is empowered to impose an administrative fine. The amount of the fine depends on the charges; for instance, not exceeding €1 million for market manipulation; not exceeding €50,000 for directors dealing without disclosure.¹⁶⁵ Under the *WpHG*, insider trading is a criminal offence. When any suspicious insider trading is found, the BaFin must report the facts to the public prosecutor's office to further investigate the case.¹⁶⁶

Unlike US law and practice, the BaFin has no power to require directors to pay damages, to seek their disqualification as a director for misconduct, or to seek injunctions to prevent future violations. In addition, the power of supervising German capital markets does not solely belong to BaFin. It has to share responsibility for supervision with individual German state bodies. To enforce securities law, BaFin has to rely on the public prosecutors. It is claimed that the staff of the corporate department of the prosecutors is insufficient and inexperienced.¹⁶⁷ Therefore, there is a suggestion to extend BaFin authority to include civil actions on behalf of the corporation and shareholders.¹⁶⁸ Despite the recommendation, given limited finance and personnel,

¹⁶⁰ Ibid § 10(1).

¹⁶¹ Bo James Howell, 'Executive Fraud and Canada's Regulation of Executive Compensation' (2007) 39 *University of Miami Inter-American Law Review* 111, 130; *Securities Supervision/Asset Management* (2012) Bundesanstalt für Finanzdienstleistungsaufsicht <http://www.bafin.de/EN/BaFin/Functions/History/SecuritiesSupervisionAssetManagement/securities-supervision-asset-management_node.html> at 20 March 2012.

¹⁶² *Wertpapierhandelsgesetz* of 1998 [Securities Trading Act] (Germany) §§ 20a, 39(1).

¹⁶³ Ibid §§ 15a, 39(2).

¹⁶⁴ Ibid §§ 21, 39(2).

¹⁶⁵ Ibid § 39(4).

¹⁶⁶ Ibid §§ 4(5), 38.

¹⁶⁷ Thomas MJ Möllers, 'Investor Protection in the System of Capital Markets Law: Legal Foundations and Outlook' (2010) 36 *North Carolina Journal of International Law & Commercial Regulation* 57, 76; Klaus J Hopt, 'Comparative Corporate Governance: The State of the Art and International Regulation' (2011) 59(1) *American Journal of Comparative Law* 62–3.

¹⁶⁸ Hopt, above n 167, 62.

BaFin may not have the competence to do so.¹⁶⁹ Due to the limited scope of its authority, it has been pointed out that BaFin may not do much to enhance minority shareholders' rights.¹⁷⁰

A radical change to BaFin is underway due to the establishment of the new European Supervisory Authorities (ESAs).¹⁷¹ These three European Union regulatory agencies consist of the European Banking Authority (EBA), the European Insurance and Occupational Authority (EIOA) and the European Securities and Markets Authority (ESMA). ESMA took over the role of the Committee of European Securities Regulators in January 2011. The core function of ESMA is to ensure a harmonisation of rules among the member states.¹⁷² ESMA is empowered to issue guidelines, recommendations, and draft regulations and to implement technical standards that are applied to all member states.¹⁷³ The power to supervise the markets however still remains with the national authorities.¹⁷⁴ ESMA has the enforcement power to ensure the consistent application of draft regulations.¹⁷⁵ It can initiate the investigation of national regulators. If a national regulator refuses to comply with the draft regulations, the matter may be referred to the European Court of Justice.¹⁷⁶ Obviously, to some extent, the power of national authorities over securities markets will be reduced. The issue of the

¹⁶⁹ Ibid 63.

¹⁷⁰ Anke Weber, 'An Empirical Analysis of the 2000 Corporate Tax Reform in Germany: Effects on Ownership and Control in Listed Companies' (2009) 29 *International Review of Law and Economics* 57, 58.

¹⁷¹ See Jacques de Larosière, 'The High-Level Group on Financial Supervision in the EU' (The European Commission, 2009); *Proposal for a Regulation of the European Parliament and of the Council Establishing a European Securities and Markets Authority* (2009) Commission of the European Communities <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2009:0503:FIN:EN:PDF>> at 20 March 2012; *European System of Financial Supervisors (ESFS): Frequently Asked Questions* (2009) Europa <<http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/09/404>> at 20 March 2012; *A New Constitution for the Financial Market System* (2009) Bill Cash's European Journal <http://www.europeanfoundation.org/my_weblog/2009/10/a-new-constitution-for-the-financial-market-system.html> at 20 March 2012.

¹⁷² *About ESMA* (2011) European Securities and Markets Authority <<http://www.esma.europa.eu/index.php?page=cesrinshort&mac=0&id=>>> at 20 March 2012.

¹⁷³ Regulation (EU) No 1095/2010 of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and Repealing Commission Decision 2009/77/EC [2010] OJ L 331/84 Article 8–9.

¹⁷⁴ *Frequently Asked Questions: A Guide to Understanding ESMA* (2011) European Securities and Markets Authority <http://www.esma.europa.eu/system/files/2011_009.pdf> at 20 March 2012, 8.

¹⁷⁵ Regulation (EU) No 1095/2010 of 24 November 2010 Article 17.

¹⁷⁶ Ibid.

role of BaFin in supervising the German market in the current convergence of supervisory securities regulators in member states will continue to be discussed.

Thailand

The Thai Securities and Exchange Commission (“Thai SEC”) is the supervisory authority of the Thai stock exchange.¹⁷⁷ Where it reasonably suspects violations of securities laws, the Thai SEC is empowered to take both administrative actions and file criminal complaints with the Department of Special Investigation (DSI) for further criminal proceedings. The administrative actions include issuing notices for rectifications, imposing warnings, probation, suspension of approval for a specified period of time, or revocation of approval.¹⁷⁸ In regard to criminal offences, if the offences have not had significant impact on the public, the Thai SEC presents the case to the Settlement Committee, appointed by the Minister of Finance, to impose fines.¹⁷⁹ The Settlement Committee comprises three members who are representatives of the Royal Thai Police Headquarters, the Fiscal Policy Office of the Ministry of Finance, and the Bank of Thailand. For offences which have had a significant public impact and cannot be transferred to the Settlement Committee,¹⁸⁰ or in which the offenders refuse to pay the fine as ordered by the Settlement Committee, the Thai SEC files criminal complaints with the DSI for further investigation and criminal prosecution.¹⁸¹ Similar to BaFin, the Thai SEC has no power to initiate a civil action against wrongdoers.

As discussed in Chapter 3, the core criticism of the Thai SEC is about its independence and integrity. In the past, the connection between the Thai SEC and the government was very strong. The Minister of Finance held the position of chairperson.¹⁸² The minister

¹⁷⁷ For a detailed discussion of the Thai SEC, see Section 3.5.

¹⁷⁸ *SEC in Brief: Inspection and Enforcement* (2009) Securities and Exchange Commission <http://www.sec.or.th/sec/Content_0000000324.jsp?categoryID=CAT0000430&lang=en> at 20 March 2012. If the offender disagrees with the decision made by the SEC, he may bring the case to the Administrative Court within 90 days after the order is made. See http://www.sec.or.th/enforcement/admin_chart.pdf.

¹⁷⁹ Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 317.

¹⁸⁰ *Ibid.*

¹⁸¹ Securities and Exchange Commission, above n 178. If the offender disagrees with the decision made by the SEC, he may bring the case to the Administrative Court within 90 days after the order is made. See http://www.sec.or.th/enforcement/admin_chart.pdf.

¹⁸² Securities and Exchange Act B.E. 2535 (1992) (Thailand) s 8.

was also empowered to appoint other members of the Thai SEC.¹⁸³ Given the strong relationship, there have been several scandals on the independence of the Thai SEC. One of the most criticised cases is the sale of shares made by the sister of the former prime minister, now the prime minister.¹⁸⁴ Recently the Securities Act was amended to limit governmental control over the Thai SEC. The Minister of Finance is no longer the chair of the Thai SEC and is no longer able to appoint members of the Thai SEC. This change may ensure the integrity of the market regulator and the market itself.

In addition to the published comments on the powers of the Thai SEC, the field research sought the views of legal practitioners on the role of the Thai SEC in supervising the Thai capital market. Regarding the integrity of the Thai SEC, one interviewee, a former professor and independent director, pointed to the potential positive effects of the recent changes:

Previously, the chairman of the members of the SEC was the Minister of Finance. As a result, all of the SEC's policies were influenced by politics. With the lack of transparency, listed companies were not confident with the SEC. Now, the chairman of the SEC is chosen by a specific committee. This will improve the integrity of the SEC in supervising the market.¹⁸⁵

A Thai SEC officer referred to personnel of the Thai SEC and their extended roles:

Personally, I think that the SEC has sufficient personnel to overlook the market operating system. The officers are knowledgeable and well understand the rules. The SEC randomly inspects financial statements of approximately 20 to 50 per cent of listed companies. Though it is not our duty, we do it as a preventive measure because there has been no report from auditors on suspected actions. The SEC cooperates well with related organisations such as the Stock Market of Thailand, the [Department of Special Investigation], and public prosecutors. The SEC also arranges continuous training programs for DSI, public prosecutors, and judges to provide equal understanding on the securities law to all enforcement agencies.¹⁸⁶

¹⁸³ Ibid.

¹⁸⁴ The details of this transaction are discussed in Section 3.5.1.1.

¹⁸⁵ Interview with a professional independent director, Bangkok.

¹⁸⁶ Interview with an SEC officer, Bangkok.

7.3.2 The roles of securities regulators: compared

The above section outlined the backgrounds to the three securities regulators. This section focuses on comparing their authority and power and seeks to explain the differences. Compared with the responsibilities of the US, German, and Thai securities regulators, the power of the stock exchange supervisory authorities in the three jurisdictions can be summarised as follows:

Table 7.1 Power of the securities regulators in the three jurisdictions

Powers	The SEC	BaFin	The Thai SEC
To take civil action for damages	Yes (The Fair Fund provision)	No	No
To disqualify directors	Yes (Imposed by the court)	No	Yes (Imposed by the SEC)
To impose civil penalties	Yes (Imposed by the court and the SEC)	Yes (In accordance with the rules for fine administration fine proceedings)	Yes (Imposed by the Settlement Commission)
To apply for injunctions	Yes	No	No
To issue administrative cease-and-desist proceedings	Yes	No	No
To take disgorgement proceedings	Yes	No	No
To prosecute	No	No	No

Source: Author's compilation

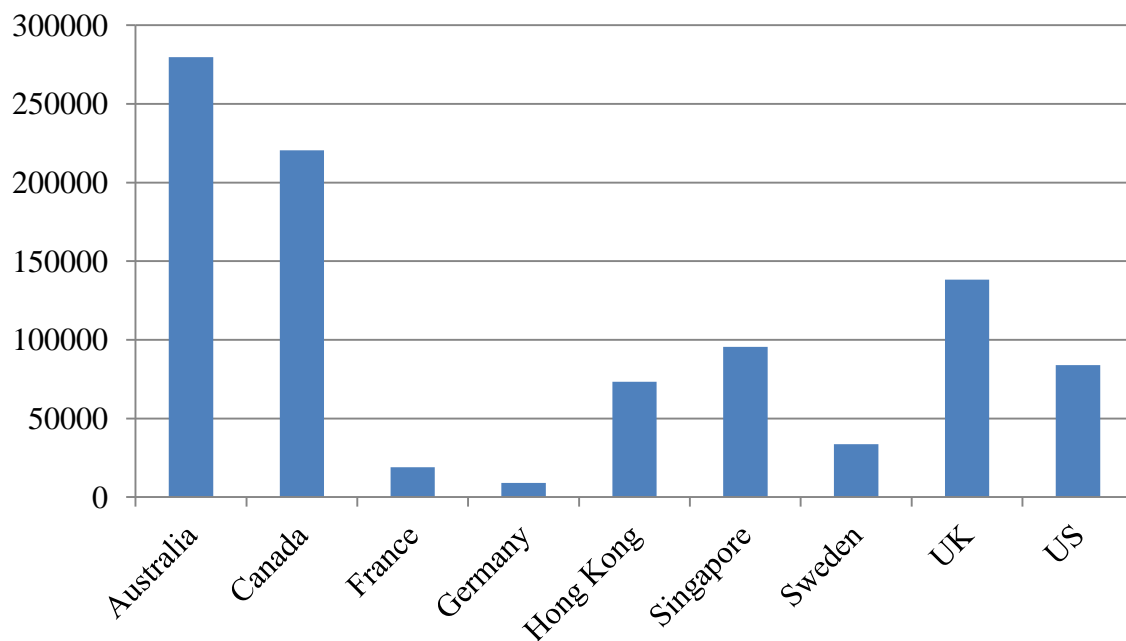
The research shows that, in studied civil law countries, the securities regulators have comparably limited power to enforce securities laws. The US regulator as the market supervisor is empowered to reimburse injured investors while the authorities in both Germany and Thailand do not have such a power. The more limited power of the securities supervisory agencies in civil law jurisdictions compared with common law jurisdictions has been noticed in the literature. Jackson concluded:

The common law countries ... report markedly higher levels of regulatory intensity on all dimensions I have studied. While many observers associate the civil law regimes with legal rigidity and bureaucratic ossification, the indicia on regulatory intensity in

financial areas suggest that it is the common law countries that carry the bigger sticks and swing them with greater frequency and force.¹⁸⁷

In observing the intensity of regulatory efforts in major industrialised countries, he found that civil law countries spend less in regulating securities market than common law countries do. Figure 7.1 illustrates.

Figure 7.1 Securities regulation costs per billion dollars of stock market capitalisation (2003–2004)

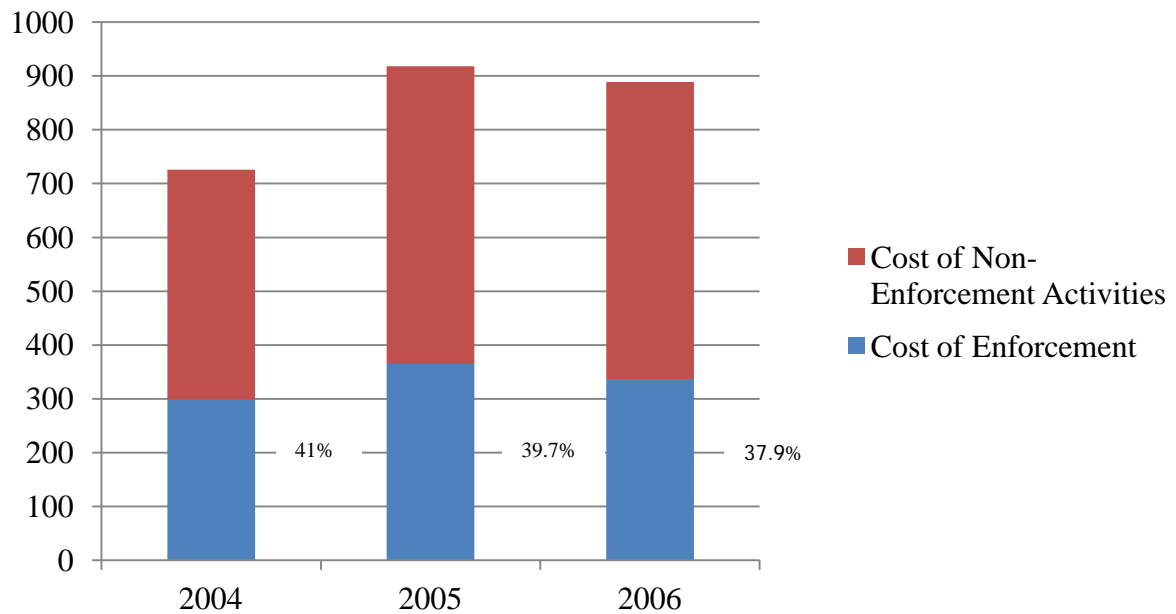


Source: Howell Jackson, 'Variation in the Industry of Financial Regulation: Preliminary Evidence and Potential Implications' (2007) 24(2) *Yale Journal on Regulation* 253, Figure 3

Observing how supervisory agencies spend their budgets on enforcement activity, Coffee found a similar result. Enforcement expenditures at the US SEC ranged between 37.9 per cent and 41 per cent of its total budget, while those at the BaFin ranged between 3.1 per cent and 6.5 per cent of its total budget. Figures 7.2 and 7.3 illustrate.

¹⁸⁷ Howell Jackson, 'Variation in the Industry of Financial Regulation: Preliminary Evidence and Potential Implications' (2007) 24(2) *Yale Journal on Regulation* 253, 256.

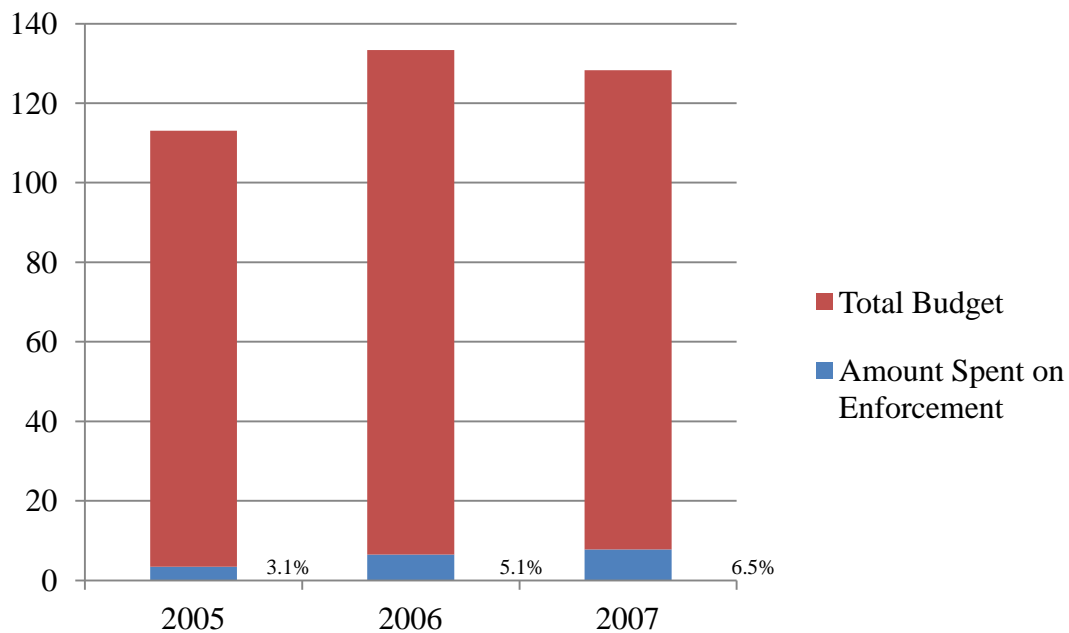
Figure 7.2 SEC enforcement activity as a percentage of the SEC's total budget (2004–2006)¹⁸⁸



Source: John C Jr Coffee, *Law and the Market: The Impact of Enforcement* (2007) 156(2) *University of Pennsylvania Law Review* 229, Figure 10

¹⁸⁸ Despite the enactment of the Dodd-Frank Act in 2010, the pattern of the budget allocated for legal enforcement of the SEC has not changed. From 2009 – 2011, 35, 34, and 34 per cent of the total budget were allocated to enforcement activities respectively. See Securities and Exchange Commission, *FY 2009 Congressional Justification* (2009) Chart 2; Securities and Exchange Commission, *FY 2010 Congressional Justification* (2010) Chart 2; Securities and Exchange Commission, *FY 2011 Congressional Justification* (2011) Chart 2.

Figure 7.3 Amount spent on enforcement by BaFin (2005–2007)



Source: John C Jr Coffee, *Law and the Market: The Impact of Enforcement* (2007) 156(2) *University of Pennsylvania Law Review* 229, Table 3

Coffee has sought to explain the different approaches between this pattern of enforcement in civil and common law jurisdictions. He claimed that the levels of ownership had a direct relationship with enforcement intensity.¹⁸⁹ In the US, where the ownership is diffused and control is in the hands of directors, enforcement actions are vital as the regulators generally learn of violations (such as insider trading) after the event. On the other hand, in civil law countries where the ownership is concentrated, a violation made by controlling shareholders is likely to be foreseen before the violation takes place and may be prevented. For instance, if a controlling shareholder desires to acquire the remaining shares from minority shareholders, the regulator can take action before the transaction has been commenced. Therefore, the cost of overseeing market activities is lower in civil law countries. In addition, the degree of pressure on politicians to strengthen legal enforcement in civil and common law countries is different.¹⁹⁰ After a series of corporate collapses in US stock markets, a large number of individual shareholders have called for better protection and this becomes a political

¹⁸⁹ Ibid 294–6.

¹⁹⁰ Ibid 297–9.

force. The Congress responded by strengthening and empowering the market supervisor to enforce securities regulations to provide better protection for minority shareholders. On the other hand, such a demand in the concentrated ownership market is less powerful. In Thailand, for example, as discussed in Chapter 3, the number of retail investors is small¹⁹¹ and the political pressure is therefore rather weak.

7.3.3 The power of the Thai SEC: reconsidered

Among the three jurisdictions, the authority of the German and Thai regulators is similar. The regulators are empowered to issue civil penalties to wrongdoers but have no authority to initiate a civil action on behalf of shareholders or companies for damages. The authority of the US regulator is significantly broader. It can issue civil penalties, apply for injunctions, take disgorgement proceedings, and importantly, take civil action for damages. The core question to consider is whether Thailand should confer some of the US SEC's powers on the Thai SEC to enhance enforcement or retain its present limited authority. If Thailand decides to extend the power of its SEC, another issue to consider is whether those powers can function within the Thai context.

As discussed earlier, private enforcement of company and securities law does not function effectively in Thailand. Although derivative actions were adopted more than 100 years ago, there has been no case brought to the Supreme Court by shareholders in a public company.¹⁹² The relevant law has recently been revised, but there is no evidence that the revision will produce any change. Unlike the US, as contingent and conditional fees are not allowed, Thai lawyers have limited motivations in acting in such litigations. The decision to make a claim solely depends on the affected shareholders. With no direct financial benefit, minority shareholders have no incentive to contribute their time or money to litigation. Class actions have not been adopted in Thai law. Therefore, there is no similar means to encourage and facilitate minority shareholders in initiating a legal action. Due to the present lack of workable remedies, Thailand should consider conferring greater authority in the Thai SEC.

¹⁹¹ See Chapter 3.

¹⁹² Information based on the search engine provided by the Supreme Court website as of March 2012 at <http://www.deka2007.supremecourt.or.th/deka/web/search.jsp>.

The first question is to what extent the powers of the Thai SEC should be extended. Similar to the US SEC, the Thai SEC is presently authorised to fine a wrongdoer and issue a director with a disqualification order. The power of the Thai SEC, however, does not include the ability to apply for injunctions or to seek to recover compensation for injured shareholders. Under Thai corporate law, only shareholders holding an aggregate number of shares not less than five per cent can request the court to prohibit directors from engaging in misconduct.¹⁹³ The research suggests that Thailand should consider allowing the Thai SEC to take a role in preventing possible violation. This is because, firstly, as pointed out earlier in this chapter, it is difficult for minority shareholders to gather sufficient votes to reach the five-per-cent requirement. Secondly, given the Thai SEC's authority in investigating corporate activities and financial statements, it is in a suitable position to detect a violation. As well, the use of injunctions is a common practice in Thai procedural law.¹⁹⁴ Extending the Thai SEC's power is unlikely to cause any confusion to corporate players. The related inquiry is which institution – the court or the Thai SEC – should have the power to issue an order to desist from future wrongdoing. The literature indicates that the power should be held by the Thai SEC. Given the different roles of courts in common and civil law countries and the long timeframes for cases in Thai legal procedure, seeking orders from the court may not be effective.¹⁹⁵ Proceeding with the allegations within the Thai SEC can shorten procedures and make legal enforcement more effective. To ensure the integrity and transparency of the order, there should be an independent body dealing with the Thai SEC's request for the order. Besides, the suspects who disagree with the Thai SEC's order should be allowed to have the court reconsider such an order.

The next issue is whether the Thai SEC should be entitled to bring a civil action against wrongdoers to reimburse shareholders who have been harmed. In practice, due to their small stakes, minority shareholders in public companies rarely bring private actions against directors. As discussed earlier, although the provision on derivative actions has been revised to encourage minority shareholders to assert a claim, it may not be as

¹⁹³ Public Limited Company Act B.E. 2535 (1992) (Thailand) s 85.

¹⁹⁴ See Civil Procedure Code B.E. 2477 (1934) (Thailand) s 254.

¹⁹⁵ In a securities case, it generally takes at least five years to have a verdict delivered. Information based on the interview with a public prosecutor, Bangkok, Thailand.

effective as it is in the US. Also, as noted, class actions do not exist. In the absence of effective private actions, the Thai SEC should play a greater role in enforcing securities laws in order to show positive effects on market supervision.¹⁹⁶ There is some, but not general support, for this amongst those interviewed. As one legal practitioner stated:

It seems that a leading role by the SEC in bringing cases would be the most effective way to add some discipline to the market, familiarise the judiciary with securities cases, and show investors that the law offers them real protection.¹⁹⁷

An investor affirmed this view. He pointed out the necessity to empower the SEC's authority:

Investors normally do not file lawsuits as their stakes are minimal. They instead sell their shares. In my opinion, taking a lawsuit should be the responsibility of the SEC. The SEC should protect minority shareholders rather than letting minority shareholders fight with the majority shareholders or managers themselves. Though the damage to each minority shareholder is minimal, the damage overall to the market as a whole is serious. This also decreases investors' confidence. Presently, the SEC is in charge of investigations. Adding lawsuits to their responsibility should not be too much for the SEC.¹⁹⁸

A legal practitioner also agreed that the Thai SEC should be encouraged to initiate such action:

My questions are whether the SEC should be authorised to file a civil case against the accused; how the damages will be distributed; whether the SEC is ready for this position. I personally think that the SEC is in the position to claim damages for minority shareholders and should claim damages for minority shareholders. If the SEC is afraid of counterclaim, a transparent and fair system should be established.¹⁹⁹

¹⁹⁶ See Winship, above n 116, 1132–3. See also Marlon Layton, 'Is Private Securities Litigation Essential for the Development of China's Stock Market?' (2008) 83 *New York University Law Review* 1948.

¹⁹⁷ John Fagan, 'The Role of Securities Regulation in the Development of the Thai Stock Market' (2003) 16 *Columbia Journal of Asian Law* 303, 341. See also Nisha Kanchanapoomi, 'Note: Accelerating Corporate Governance Reform in Thailand: The Benefits of Private Reform Mechanisms' (2005) 15 *Southern California Interdisciplinary Law Journal* 165; Obeua S Persons, 'Governance in Thailand: What Has Been Done Since the 1997 Financial Crisis?' (2008) 11(2) *Thailand Law Journal* <<http://www.thailawforum.com/Volume11fall08.html>> at 20 March 2012.

¹⁹⁸ Interview with an investor, Bangkok.

¹⁹⁹ Interview with a public prosecutor, Bangkok.

However, a Thai SEC officer had a different view, partly because of the Thai SEC's limited resources:

I think bringing an action against misconduct directors is not the role of the market supervisor but the shareholders themselves. Giving the power to the SEC can cause many problems, ie, how such power should be employed. Besides, this can have a serious effect on the [SEC]. For example, if the injured parties are not satisfied with the SEC's solution, they may sue the SEC for making a wrong decision.²⁰⁰ To initiate a legal action, it includes both investigation and litigation. The SEC can investigate but does not have enough staff for litigation.

A lawyer, a former Thai SEC officer, who often works for corporate management, supported this view:

I disagree that the SEC should have authority to file a lawsuit because: (1) the DSI already has the authority to inspect cases; (2) the SEC is not ready to be a law enforcement agency; (3) to allow the SEC to inspect and file a lawsuit themselves will overburden them. My suggestions are (1) there should be cooperation among law enforcement agencies; (2) law enforcement agencies must be better educated in relation to securities law. It is my assumption that, if the law enforcement agencies understand the law in the same way, enforcement will not be complication and will be successful.²⁰¹

Although there is a perceived need to empower the Thai SEC to initiate a court action, the Thai SEC is not yet seen – because of the knowledge and skills of its staff and resources – as being able to do so.

If the proposal on extending the Thai SEC authority is accepted, apart from the concern of sufficient skilled personnel and resources, it is necessary to understand that, together with resources and skilled staff, the operation of the SEC is supported by other legal tools, such as plea bargaining. In a criminal prosecution this permits the accused to negotiate a mutual agreement with the prosecutor to plead guilty in exchange for a lesser charge or the original criminal charge with a recommendation of a lighter

²⁰⁰ Interview with a Thai SEC officer, Bangkok.

²⁰¹ Interview with a corporate lawyer, Bangkok.

sanction.²⁰² Both parties benefit from plea bargaining.²⁰³ It reduces the number of cases in the court. It ensures a conviction for prosecutors. The accused benefits from the reduced charge and lesser penalty and avoids the high costs of trial. Despite its advantages, most scholars oppose plea bargaining, finding it inefficient and unjust.²⁰⁴ US courts, however, have accepted it. In practice, in approximately 95 per cent of white-collar convictions there are guilty pleas.²⁰⁵ Plea bargaining facilitates the operation of the SEC as, firstly, the SEC can finalise the cases faster. Secondly, the information provided by the accused may be used against other suspects or in other cases. This approach, however, is not recognised in Thai legal culture. The prosecutor has no authority to negotiate with the defendant to reduce the charge. If the defendant confesses, that confession will be used as evidence. The court may reward the defendant with a reduction in the sentence.²⁰⁶ In practice, the defendant in white-collar cases rarely pleads guilty. This is because plea bargaining is not allowed. Besides, given the high burden of proof, prosecutors rarely win securities cases. Consequently, the Thai

²⁰² For a discussion on plea bargaining, see Albert W Alschuler, 'Implementing the Criminal Defendant's Right to Trial: Alternatives to the Plea Bargaining System' (1983) 50 *University of Chicago Law Review* 931; Steven P Grossman, 'An Honest Approach to Plea-Bargaining' (2005) 29 *American Journal of Trial Advocacy* 101; Russell Covey, 'Fixed Justice: Reforming Plea Bargaining with Plea-Based Ceilings' (2008) 82 *Tulane Law Review* 1237.

²⁰³ See Raymond McKoski, 'Judicial Discipline and the Appearance of Impropriety: What the Public Sees is What the Judge Gets' (2010) 94 *Minnesota Law Review* 1914, 1789–81.

²⁰⁴ See Albert W Alschuler, 'The Defense Attorney's Role in Plea Bargaining' (1975) 84 *Yale Law Journal* 1179; Albert W Alschuler, 'The Trial Judge's Role in Plea Bargaining' (1976) 76 *Columbia Law Review* 1059; Stephen J Schulhofer, 'Is Plea Bargaining Inevitable?' (1984) 97 *Harvard Law Review* 1037; Stephen J Schulhofer, 'Plea Bargaining as Disaster' (1992) 101 *Yale Law Journal* 1979; Russell Covey, 'Signaling and Plea Bargaining's Innocence Problem' (2009) 66 *Washington & Lee Law Review* 73.

²⁰⁵ Table 7.2 Guilty pleas and trials in selected white-collar categories

Crime	Year	Plea per cent	Trial per cent
Fraud	2007	95	5
	1997	94.1	5.9
Embezzlement	2007	97.6	5.4
	1997	97.5	2.5
Bribery	2007	89.7	10.3
	1997	90.6	9.4
Environment/Wildfire	2007	96.9	3.1
	1997	94.7	5.3
Antitrust	2007	100	0
	1997	81.8	18.2
Food & Drug	2007	97.2	2.8
	1997	91.9	8.2

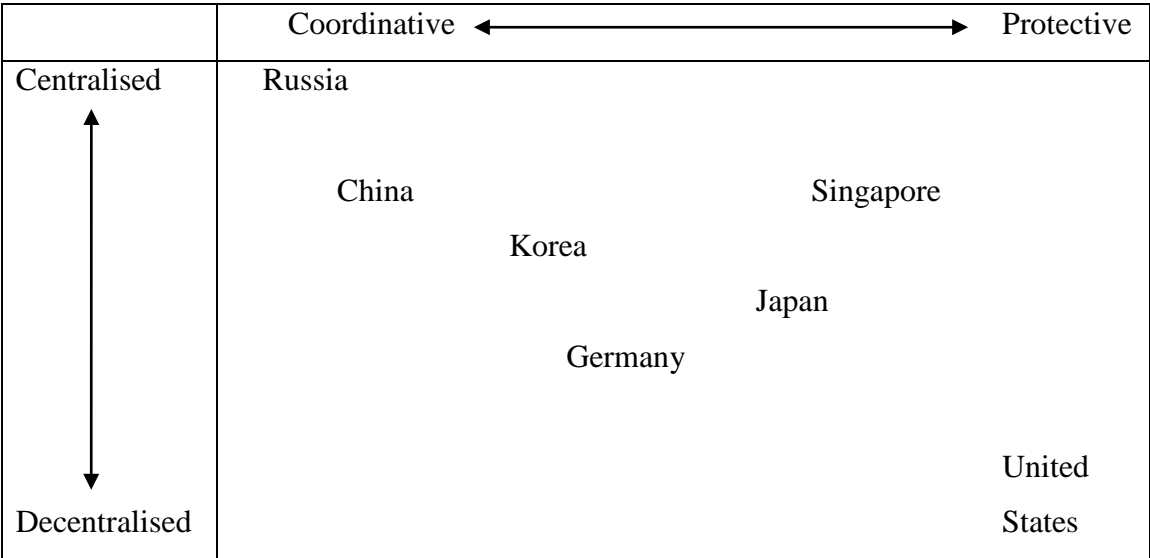
Source: Ellen S Podgor, 'White Collar Innocence: Irrelevant in the High Stakes Risk Game' (2010) 85 *Chicago-Kent Law Review* 77, Appendix

²⁰⁶ Criminal Code B.E. 2499 (1956) (Thailand) s 78.

SEC has to spend a significant amount of its time and resources working on a limited number of cases.

In addition to plea bargaining, the other significant factor driving strong enforcement in the US is the attitude to litigation. As pointed out by Milhaupt and Pistor, the US has the most decentralised and protective legal system.

Figure 7.4 Legal systems’ matrix



Source: Curtis J Milhaupt and Katharina Pistor, *Law and Capitalism: What Corporate Crises Reveal about Legal Systems and Economic Development Around the World* (2008) Figure 9.1

In the US, legislation reflects a policy of supporting strong legal regulation. Together with private enforcement, the SEC plays a significant role in protecting investors. Frequently, the power of the regulator becomes stronger after an economic crisis. This is evidenced from the Wall Street crash in 1929, through the corporate failures in 2001, and the current financial crisis in 2008. The same pattern is not seen in Thailand. Even after the financial crisis in 1997, the idea of empowering the Thai regulator to protect investors has not been on the agenda. Interviews with Thai legal practitioners also show unshakable resistance to public enforcement by Thai regulators being strengthened. This is a significant impediment to further regulatory reform.

Given the difficulties of strengthening the power of the Thai SEC, it may be of benefit to Thailand to consider further developing new governance models of regulation. One of the new regulatory practices includes the utilisation of soft law to complement mandatory hard law.²⁰⁷ Soft regulation is the use of non-binding rules and practices, such as a voluntary code of conduct. A company employs the code as benchmarks to institute its own codes of conduct to regulate its operations. Given its flexibility, the codes can adapt faster to changing business norms than mandatory rules.²⁰⁸ In exchange, the company enjoys other benefits.²⁰⁹ It, firstly, can attract the investors' attention. Secondly, the regulator may grant a reward for firms that accept voluntary obligations. This regulatory approach mainly relies on economic and social pressure from consumers and commercial benefits rather than coercive enforcement.²¹⁰ Despite the lack of enforcement, corporations comply with soft law to ensure their reputational accountability.²¹¹ It is claimed that the 'psychological effects of soft regulation can cause even regulated actors to go beyond the minimum required by the law'.²¹²

Overall, the different ownership structures and the role of politicians have led to US law providing a wider range of power for the securities regulator than those found in German and Thai law. The findings show that some of the US legal tools, such as injunctions and civil actions could be employed in Thailand to strengthen legal enforcement and enhance minority shareholders' protection. The adoption of the injunction is possible, as this concept already exists and is used in the Thai legal system. Although civil actions could benefit minority shareholders, as private enforcement in Thailand is ineffective successfully, adopting such a concept into the Thai legal system is not a simple task.

²⁰⁷ For a discussion on the concept of soft law, see Gunther F Handl et al, 'A Hard Look at Soft Law' (1988) 82 *American Society of International Law Proceedings* 371; Anna di Robilant, 'Genealogies of Soft Law' (2006) 54 *American Journal of Comparative Law* 499.

²⁰⁸ Caroline J Dillon, 'Do You Get What You Pay For? A Look at the High Fees and Low Protections of Mutual Funds' (2006) 2006 *Columbia Law Review* 281, 307.

²⁰⁹ Kenneth Abbott and Duncan Snidal, 'Strengthening International Regulation Through Transnational New Governance: Overcoming the Orchestration Deficit' (2009) 42 *Vanderbilt Law Review* 501, 530–1.

²¹⁰ *Ibid* 543.

²¹¹ Kevin T Jackson, 'Global Corporate Governance: Soft Law and Reputational Accountability' (2010) 35 *Brooklyn Journal of International Law* 41, 89–90.

²¹² Dillon, above n 208, 307.

7.4 Conclusion

The remedies available to Thai minority shareholders are very limited. The absence of effective legal enforcement may explain why they behave as speculators rather than as investors. Derivative actions have been incorporated into the Thai legal system for a long time, but in practice, minority shareholders are unlikely to bring such an action due to a lack of direct financial interest. The transplant of derivative actions shows that, without parallel changes in other parts of the legal system, such as the contingent fee arrangements for legal practitioners, the adopted rule cannot function the way it does in the system from which it is borrowed. Class actions, which would be more efficient and effective for minority shareholders, as a group are also not permitted under Thai law. Even if they were in the absence of contingent fees or litigation funding they may also not be effective. The regulator also has no authority to take civil actions to cover damages on behalf of shareholders. Given the absence of shareholder litigation, the research indicates the need to extend the Thai SEC's power to include recovering damages for shareholders. However, given the limitation of the Thai SEC's personnel and resources and Thai legal culture more generally successful public enforcement will not be easy to achieve. Even if such a public remedy were to be provided to minority shareholders through Thai SEC it may not be effective. Such legal transplants are not easy. The issue of legal transplants in Thai company law is covered in the next chapter.

Chapter 8

Transplanting Corporate Law: Thailand's Experience

- 8.1 Introduction
- 8.2 The possibility of legal transplants: the experience from Thai company law
- 8.3 The success of legal transplants
- 8.4 Where to from here?
 - 8.4.1 Adopting the German dual board model
 - 8.4.2 Maintaining common law transplantation
 - 8.4.3 Strengthening Thai corporate law and regulation
 - 8.4.3.1 Family-owned companies
 - 8.4.3.2 Independent directors
- 8.5 Conclusion

8.1 Introduction

The previous chapters have described and compared the laws of the United States, Germany, and Thailand on minority shareholders' protection, including the rights of minority shareholders, the duties of directors and controlling shareholders, the protection of minority shareholders in specific contexts, and the remedies available to them. This chapter considers the possible applicability of US and German corporate law to the Thai local context. One of the research questions relates to transplanting law. This raises the justifications for adopting or adapting of laws from the US or Germany to Thailand, the obstacles to that, and the feasibility of applying these laws in the Thai context. This chapter begins with a discussion on the possibility of legal transplants, focusing on transplants in Thai company law. It also examines the success of the transplants which have occurred and suggests a model for reform in Thai company law.

8.2 The possibility of legal transplants: the experience from Thai company law

As discussed in Chapter 3, the idea of transplanting legal concepts and ideas from one legal system to another is not new. The questions of whether such concepts or ideas from one legal system can be transplanted into another legal system, why attempts are

made to transplant law, and whether legal transplants can be successful, have been discussed for at least 300 years in Western Europe. Opinions on all of these issues vary. Drawing on literature, this section examines, from Thailand's experience, whether legal transplants are possible.

As indicated, the Thai government's drive to revise company and securities laws is based on the belief that the changes would advantage the Thai economy. This reflects Watson's argument that the adoption of foreign legal concepts is driven by the desire of lawmakers. The lawmakers believe that a foreign law would be beneficial so transplant it.¹ Kahn-Freund also claimed that interest groups, including law makers, were significant in promoting legal transplants. They may be significantly insisting in transplants depending on whether the transplant would advantage or disadvantage them.²

Watson accepted that law is easily transplanted. Montesquieu, Kahn-Freund and Legrand, among other writers, had questioned the possibility of legal transplants. They have pointed out that legal rules do not stand alone, but are deeply attached to the social structure. Transplanting a rule from a jurisdiction that has no similar elements to a recipient jurisdiction is unlikely to be successful. The Thai experience in the early use of company law affirms these views. As discussed, in 1889 the Thai government adopted the concept of company to separate the legal personality of the company from its shareholders and managers. Thai legal practitioners were not familiar with this concept.³ They believed that the managers were a part of the company and *vice versa*. The idea of a separate legal personality was entirely new to them. However, the confusion did not end the development of Thai company law. Although there was no legislation relating to companies, Thai judges, who were educated in England adopted

¹ Alan Watson, 'Legal Transplants and Law Reform' (1976) 92 *Law Quarterly Review* 79, 79.

² As pressure groups they shape the idea of national officials and are also influential, as legal agents, in how such laws are adapted and implemented. Kahn-Freund went further than Watson in recognising the importance of these elites in explaining resistance and acceptance between donors and hosts. Otto Kahn-Freund, 'On Uses and Misuses of Comparative Law' (1974) 37(1) *The Modern Law Review* 1, 12–3, 27. See Alan Watson, *Legal Transplants: An Approach to Comparative Law* (1974) 96–7; Yves Dezalay and Bryant G Garth, 'The Import and Export of Law and Legal Institutions: International Strategies in National Palace Wars' in David Nelken and Johannes Feest (eds), *Adapting Legal Cultures* (2001) 241–56.

³ Tipchanok Ratanosoth, *Partnership and Company Laws* (2010) 187.

English company law to resolve corporate conflicts in their courts.⁴ As indicated, Thai company law was then codified in 1911 and has since further developed.

A reason for the possibility of the transplant of company law may be the nature of company law itself. The contractarian theory views a company as a series of agreements among participants – among shareholders and between shareholders and directors.⁵ Company law is thus a transaction facilitator. Instead of negotiating each contract, it institutes a set of default rules so that parties can enter into a contract quickly and inexpensively. The idea of facilitating business transactions is well known to commercial lawyers and they may have been supportive of its adoption and use for this reason. This literature also shows that company law may have less connection with social and historical contexts of a particular society compared with other laws. As pointed out by Teubner, law that is loosely coupled with social processes is more easily transplanted than law that is more tightly coupled.⁶ Compared with family and criminal law, company law may be more easily detached and transferred.

Another explanation may be the close connection between the adopted rules and local legal practitioners. According to Berkowitz *et al*, in addition to the demand for law, a legal transplant is likely to work if the local agents are already familiar with the basic principles of borrowed rules.⁷ As already indicated, Thai judges had a good understanding of company law. This was because due to strong relations with the United Kingdom led to a number of members of the royal family and other elite families being educated in England and studying English law.⁸ Some of them later became judges. The first law school was founded in 1897 under the leadership of Prince Rapee who was educated in England. Most of the other lecturers had been admitted as English

⁴ Sunee Mullikaman et al, 'Revolution of Thai Law in Two Centuries' (Chulalongkorn University, 1982) 152.

⁵ The discussion on the contractarian theory is in Chapter 5.

⁶ Gunther Teubner, 'Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences' (1998) 61 *Modern Law Review* 11, 19.

⁷ Curtis J Milhaupt, 'Beyond Legal Origin: Rethinking Law's Relationship to the Economy – Implications for Policy' (2009) 57 *American Journal of Comparative Law* 831, 167–8.

⁸ Central Intellectual Property and International Trade Court Thailand, 'The Judicial System in Thailand: An Outlook for a New Century' (IDE Asian Law Series No 6, Institute of Developing Economies, 2001) 56.

barristers. The curriculum, texts, and teaching style were based on English model.⁹ This benefited the early development of Thai company law as the application of the adopted rules was done by those who are familiar with the law. Merchants also drove the demand for chartered companies.

In summary, formal legal transplants into Thai company law have been proved possible. The main factor driving such transplants has been the Thai political elites. They believe that the adoption could bring some advantages to Thailand in both economic and political forms. Transplanting commenced in 1889 and appears to have flourished for the reasons given. Although formal transplants have proved possible, their success is questionable. The local legal agents are familiar with common law rules but other general rules and legal processes are largely influenced by civil law. Also, after Thailand decided to adopt a civil law system legal education and training moved towards a civil law style. In these circumstances the transplants may be less successful or have unintended consequence. The following section focuses on this.

8.3 The success of legal transplants

As mentioned, Thai company law has been adopted from the common law system but the Thai legal and regulatory systems largely derive from French and German civil law models. Given these different legal origins, it is questionable how effectively Thai corporate law functions, and whether transplanted corporate law principles function in similar or dissimilar ways to their origin.

Evaluating the success of legal transplants is not an easy task. As Nelken pointed out:

Success from one point of view does not necessarily entail success from another. What we witness, when legal change does lead to social change, is a radiating set of intended and unintended outcomes. ... [I]t is important to notice that the question of success can arise in more than one stage of the transfer of legal rules and institutions. We may be concerned with how a legal adaptation emerges—the choice of law—or with the way it exerts its influence—the results of a given transfer. Our way of explaining the first of

⁹ Ibid 56.

these matters many will be different from the second, likewise our assessment of what “success” means in each case.¹⁰

There are conflicting views on the effectiveness of transplants. Watson believed that laws could be located into different contexts. Similar to human organ transplants, a legal transplant was successful when it grew in the new body and became part of it in the same way as it did in the donor system.¹¹ Friedman also proposed that most legal transplants were likely to be successful. Borrowed rules would be reshaped by local legal professionals to make them suit the local conditions.¹² Teubner, however, suggested that the borrowed law would not function as it did in its original jurisdiction.¹³ Instead, it would irritate the legal system into which it had been transplanted and a series of evolutionary changes within the system would occur.¹⁴ Legrand argued that the meaning of a law derives from its social context so that transplants are unlikely to be successful.¹⁵ Similarly, Pistor suggested:

For law to play a role in economic activities and long-term economic development, it must be incorporated, meaning that it must develop solutions to problems that exist in the home jurisdiction.¹⁶

As this literature reveals, there is no agreement on how to evaluate the success of legal transplants. To evaluate the achievement of transplants into Thai corporate law one measure is whether the adopted rules have served their purpose – protecting minority shareholders in Thai companies. From the analysis in the previous chapters, the adopted rules that have been successfully transplanted include: the right to obtain information on the agenda to be voted on at the shareholders’ meetings; the right to vote by proxy; the rights as shareowners; and, protection in specific contexts including mergers, acquisitions, and related-party transactions. These rules function to provide protection

¹⁰ David Nelken, 'Towards a Sociology of Legal Adaption' in David Nelken and Johannes Feest (eds), *Adapting Legal Cultures* (2001) 37, 39.

¹¹ Alan Watson, *Legal Transplants: An Approach to Comparative Law* (1974).

¹² Lawrence M Friedman, 'Some Comments on Cotterrell and Legal Transplants' in David Nelken and Johannes Feest (eds), *Adapting Legal Cultures* (2001) 96.

¹³ Teubner, above n 6, 12.

¹⁴ *Ibid.*

¹⁵ Pierre Legrand, 'What "Legal Transplants"?' in David Nelken and Johannes Feest (eds), *Adapting Legal Cultures* (2001) 60.

¹⁶ Katharina Pistor et al, 'Evolution of Corporate Law and the Transplant Effect: Lessons from Six Countries' (2003) 18(1) *The World Bank Research Observer* 89, 109.

for minority shareholders. The factors for success are, firstly, that they are often procedural, a process for a company to comply with. This makes the transplant relatively easy to implement. This is consistent with Teubner's thesis that law which is loosely coupled with social processes is comparably easier to transfer.¹⁷ Also, controlling shareholders will facilitate the implementation of the process. For instance, if the controlling shareholders wish to pass a resolution in which they have an interest and from which they will benefit, they will ensure that the processes are correctly complied with. Failure to follow a clear procedure to pass resolutions entails the risk of them being revoked by the court.

The rules that have not been successfully transplanted include shareholders' proposals; derivative actions; nomination committees; and, fiduciary duties of directors. The research finds that the factors impeding the implementation of shareholders' proposals and derivative actions are, firstly, the five per cent requirement. As discussed in Chapters 4 and 7, it is difficult for minority shareholders in Thai companies to meet this requirement as it does not fit with shareholding patterns in Thai companies. Secondly, there is no incentive for them to exercise these rights. Regarding the nomination committee, the key concept is the independence of the members of the nomination committee. As discussed in Chapter 4, due to the close connections between Thai business people, it is not easy to ensure an arm's length relationship among the members of the nomination committee and the company. The fiduciary duties of directors provide the last example although they have existed in Thai law since 1911. To implement this, a series of cases need to be brought to the court as only the judges are able to define the scope of these duties through their decisions on a case-by-case basis. In Thailand, there has never been a case in the Thai Supreme Court on the duties of directors in public companies.

Although these concepts have been transplanted into Thai company law, they cannot function in the same way they do in the systems from which they come. This may be explained by the differences between the economic and social system in which Thai and Anglo-American listed companies, respectively, are located. The concept of minority

¹⁷ Teubner, above n 6, 12.

shareholders, underlying the common law model, has been developed under the influence of agency theory.¹⁸ A number of mechanisms have been created to protect minority shareholders as the control over the company shifted to management. Together with the market for corporate control, these different mechanisms seek to ensure that the management's decisions will not adversely affect the interests of the minority shareholders. In Thai companies, the conflict, because of concentrated ownership, is between controlling and minority shareholders. Some of the adopted legal rules are therefore not practical in the Thai context. Additional rights are provided to minority shareholders in the belief that they will exercise them to protect themselves. However they have no incentive to do so and limited ways to do so within the Thai legal system. Given the large shareholding of controlling shareholders, minority shareholders will see that it is impossible to remove the directors appointed by controlling shareholders, or to overcome the power of controlling shareholders. In addition, the law relating to Thai lawyers and the funding of litigations also restricts their use. Unlike in US legal practice, a contingency fee is not allowed to be charged by Thai lawyers. They cannot take a percentage of any judgment. Litigation funders are also not permitted. Without a direct financial interest, minority shareholders and lawyers have no interest in initiating litigation over mismanagement. These findings accord with Legrand's thesis. As he points out, for a successful transplant the rule has to have a close connection with its original context.¹⁹ Without a similar background the adopted rules cannot function in the way they do in the system of origin. It also confirms a point made by North in the context of law and economic development debates. He claimed that a borrowed law to be effective there had to be, in the recipient legal system, compatible dispute resolution, debt enforcement, and bankruptcy procedure.²⁰

There is also little evidence that any of the adopted rules are irritating either the legal system or other systems in Thailand at this stage.²¹ The irritations in the Thai legal system may not be evident but could develop in difficult to predict ways.²² Part of the

¹⁸ The discussion on the agency theory and the mechanisms developed under the Anglo-American approach is in Chapter 2.

¹⁹ See Legrand, above n 15.

²⁰ Douglass C North, *New Institutional Economics and Third World Development* (1995) 17–27.

²¹ For the legal irritation theory, see Teubner, above n 6, 12.

²² Ibid.

recent political instability in which party conflict has split into street violence represents a backlash against some groups of society perceived to be economic and economical elite.²³

As discussed in Chapter 3, Thai investors are mainly short-term speculators rather than long-term investors. This may be because they realise that the rules on minority shareholders' protection are not workable and so their investing behaviour established before the reforms of 1992 and 2008 continue. Fagan pointed out the factors influencing the behaviour of Thai investors to speculate is rational:

I disagree with the notion that Thai retail investors are acting irrationally when they speculate on the market, and that if they were more sophisticated they would instead invest in well-governed companies. Thai retail investors are already making rational investment decisions, given their limited resources, the nature of the market, and the lack of securities enforcement. For a Thai retail investor, speculation with little fundamental analysis is the way to maximize the potential value of their securities transactions on the SET. Because there is little market discipline and no practical legal recourse if they are defrauded, they must reduce their risk by putting little money in and getting out quickly.²⁴

Without sufficient protection provided to them by the legal transplants, minority shareholders manage their investment risks by speculation.

Overall, some adopted rules on minority shareholders' protection can be properly transplanted into the Thai local context, while others cannot. Where there is no opposition from controlling shareholders, adopted rules that are less coupled with other social, legal and regulatory processes are comparably easy to be transferred. But where these are not present, legal transplants are unlikely to be successful.

²³ See, generally, on the potential for such a backlash, Amy Chua, *World on Fire* (2003).

²⁴ Fagan, John, 'The Role of Securities Regulation in the Development of the Thai Stock Market' (2003) 16 *Columbia Journal of Asian Law* 303, 343.

8.4 Where to from here?

As indicated in the previous section, Thai company law has been mainly influenced by common law principles and rules but immersed in a civil law system. Some rules have been able to take and develop; however, other rules have not been able to. It is uncertain to which legal system Thailand should look for effective legal transplants. Given the similar legal heritage and corporate structures, German legal concepts may be a better source for improving protecting the interest of Thai minority shareholders.

8.4.1 Adopting the German dual board model

As indicated in Chapter 2, large German companies have a strong system of internal control, including a supervisory board and other forms of employee participation. The purpose of a supervisory board is to have an independent group overseeing the management board in the interests of all stakeholders and the public. The concept of co-determination, which allows the workers to participate in the management, is based on the belief that having labour and management work together would decrease the divergence between these two classes. Although such a concept can improve legal protection for minority shareholders in Thai companies, it is questionable whether adopting it into the Thai legal system is possible.²⁵

The concept of employee participation is only weakly recognised in Thailand. It was formally addressed by SET in 2006. A listed company is required to have a clear policy on the fair treatment of each and every stakeholder and provide a mechanism involving stakeholders to improve corporate performance. In practice, boards of directors do issue corporate policies on stakeholder engagement. However, such policies have hardly been implemented.²⁶ Neither Thai company law nor labour law provide any channel for employees to participate in corporate governance, in determining corporate policy or

²⁵ The concept of co-determination is adopted by China but it does not seem to be successful. Chinese listed companies are required to adopt the two-tier board structure, similar to the German model; however, one argues 'China does not have the deep roots that it does in Germany, especially in relation to employee participation'. Julian Roche, *Corporate Governance in Asia* (2004) 77.

²⁶ See Suthisak Kraisornsuthasinee, *The Relationship between Corporate Governance and Corporate Environmental and Social Performance* (2008) Stock Exchange of Thailand <http://www.set.or.th/th/regulations/cg/files/doc_seminar/2006/CGESP_Executive_Summary.pdf> at 20 March 2012.

overseeing it. Under the Labour Relations Act, a company which has more than 50 employees may set up an employee committee and arrange a meeting with such a committee every three months in order to protect employee benefits and promote good relations between employees and employer.²⁷ The employees may also form labour unions with the objectives of negotiating with the employer and to protect the interests of all employees.²⁸ However, the purpose of setting up the committee and the union is to protect the interests of employees and to ensure good relations between employees and employer rather than encouraging employees to take part in management.

In addition, similarly to other Asian countries, the relationship between management and labour is different from that of Germany. Fukuyama pointed out that, as in a number of other countries, German family businesses dominated a large part of the German economy.²⁹ However 'the family has never constrained the creation of large, professional managed firms to the degree it has in China, Italy, France, or even Britain'.³⁰ For instance, the German Stollwercks company, originally a family-owned business, hired a large professional management team to run the business.³¹ Later the company became a large enterprise. Cadbury in Britain, to the contrary, retained power within the family and remained smaller. In Thai family-controlled companies there is a clear distinction between corporate insiders and outsiders.³² Insiders, particularly family members, have unconditional and automatic trust, while outsiders must work very hard to earn that trust. Although professional managers are necessary for the successful management of these companies, the founders and controlling shareholders prefer to train their family members by educating them overseas for management positions on their return.³³ The family wealth and its control are generally retained within the family.³⁴ For outsiders it is more important for them to show their trustworthiness and absolute loyalty, rather than productivity.³⁵ Employees mainly follow directions and

²⁷ Labour Relations Act B.E. 2518 (1975) (Thailand) ss 45, 50.

²⁸ Ibid s 98.

²⁹ Francis Fukuyama, *Trust: The Social Virtues and the Creation of Prosperity* (1995) 216.

³⁰ Ibid 217.

³¹ Ibid 213.

³² Michael Backman, *Asian Eclipse: Exposing the Dark Side of Business in Asia* (1999) 74.

³³ Ibid 75.

³⁴ Ibid.

³⁵ Ibid 71–2.

take no part in management.³⁶ Some writers claim that employees expect their employer to look after them as parents would.³⁷ They also claim that employees also respect their employer and those in senior management.³⁸

During the course of the interviews conducted for this thesis, interviewees were asked about the possibility of the adoption of employee participation in Thai corporate governance. All of the interviewees disagreed with labour participation in management.³⁹ A legal practitioner emphasised the potential for conflicts of interest, which is not without irony in the Thai context of family dominated firms:

I totally disagree with the idea of having employees in the management level as there will be more disadvantages than advantages. It is necessary to understand that Thai labour are mainly not professional, especially the blue-collar ones. Giving them the power to take part in management may have a severe consequence to the company. For instance, the management may want to replace some of the employees with machines to reduce costs. This decision benefits everyone – the company and all shareholders – except workers. If we allow employees to take part in management, such a plan will definitely be opposed by the employees. My concern is how to deal with the issue of conflicts of interest.⁴⁰

Another legal practitioner who saw some benefits in the practice, in the end agreed with that view. He repeated a criticism made of workers' participation in supervisory boards in Europe, that employees did not have the skills to be involved in management:

The concept of labour participation may improve corporate governance at the firm level. Practically, companies do not pay much attention to the role of employees. The benefits received by the company normally go to the owners without consideration to employees. Not only the companies, the government itself also does not view employees' participation as important. However, if we accept the concept of co-determination, the first question we need to answer is whether Thai employees are capable of supervising management. In my point of view, I think we are still far away

³⁶ Ibid 71.

³⁷ Jintana Boonbongkarn, *Business Environment* (2009) 135. See also Philip Hughes and Brian Sheehan, *Culture and Business Practices: Two Cross-Cultural Case-Studies* (1993) Section 4.

³⁸ Boonbongkarn, above n 37, 41–7.

³⁹ It should be noted that no representatives of employees or unions were interviewed.

⁴⁰ Interview with a corporate lawyer, Bangkok.

from reaching that stage. Although employees are not allowed to take part in management, they already have their ways to exercise their rights under labour law.⁴¹

A professional independent director revealed some of adversarial aspects of Thai industrial culture. He also repeated a frequent criticism of workers' representatives on supervisory boards in Europe, that they cannot be independent of management:

Under Thai corporate culture, the role of employees is clearly separated from the role of the management. Workers are in the operational level, not the management level. They work under the management's policies and instructions. Employees must not interfere at management level as that is the power of management. If they want to take part in the management level, they may change their positions as employees to shareholders. A number of large listed companies have [Employee Stock Ownership Plan] schemes which can be considered as profit-sharing plans between the company and the employees. The other pathway that allows employees to raise their voice is through a union. Unions can be very strong and too powerful, especially in publicly owned enterprises. Some unions are reasonable and helpful but some are negative and disagreeable. In some enterprises, there are even more than one union which usually disagree with each other. I cannot see a clear advantage of having employees' representative in the board. Having employees in the board can make [the management and the workers] understand each other but such understanding can be achieved by other more efficient means such as the arrangement of the meeting between an employer and employees representatives. In the company of which I am a director, for example, we encourage employees to consider themselves as significant parts of the business. Their feedback to management are welcomed and required so that the management can have an opinion from the operational level. Some may suggest having employees' representatives involved with management in becoming a member of the audit committee or an independent director. I disagree. From my experience, employees are under the influence of directors. From what I have seen, employees do not seriously fight against directors.⁴²

Given the different economic and social circumstances of Thai law, the resistance to labour involvement in management, and the concern over the power of trade unions,

⁴¹ Interview with a corporate lawyer, Bangkok.

⁴² Interview with a professional independent director, Bangkok. His view accords with the literature discussed in Chapter 2 which argues that employee participation does not necessarily protect the interests of minority shareholders.

supervisory boards with workers' representatives and co-determination are unlikely to be adopted. Nevertheless, Thailand may consider adopting some other concepts from German law and practice that could provide better protection for minority shareholders. Firstly, as indicated in Chapter 5, German law pays closer attention to transactions between companies in a group. Both *de facto* and *de jure* related companies must disclose transactions within the group and ensure that such transactions are fair and in the interests of the relevant companies. If a controlling enterprise causes any damage to a controlled company,⁴³ the controlling enterprise, together with its management board, will be liable to the shareholders in the controlled company for any resulting damages.⁴⁴ This concept is relevant to Thai business practice as Thai listed companies are generally part of a group. The requirement for disclosure and approval of transactions among companies in the same group can deter controlling shareholders from exploiting a company's assets by transferring resources from one company to another.

Secondly, an equivalent to the electronic Federal Gazette (*Elektronischer Bundesanzeiger*), which allows communication among individual shareholders, may benefit minority shareholders in Thai companies. In Thailand, a forum called Investors' Community has been established by the Stock Exchange of Thailand Group at www.settrade.com allowing individual investors to post their comments regarding investments in the Thai stock market.⁴⁵ This forum was not created for the purpose of allowing the shareholders to communicate among themselves or of encouraging them to raise issues at a shareholders' meeting or in a court in the name of the company. Given the minimum shareholding requirements for using significant processes for protecting minority shareholders, such as the five per cent shareholding for proposing an additional agenda item at a shareholders' meeting or initiating derivative actions, an affordable and timely method of assisting shareholders to pool their votes should be provided.

⁴³ *Aktiengesetz* of 2009 [Stock Corporation Act] (Germany) § 371(3).

⁴⁴ *Ibid* § 317(1).

⁴⁵ See http://www.settrade.com/C20_Community_Main.jsp. Last visited at 3 April 2012.

8.4.2 Maintaining common law transplantation

Another issue to be considered is the continued adoption of common law practices and rules often under the guise of international standards. As mentioned earlier, common law has been adopted into Thai company law since its first use of the concept of company. However, it is clear that some common law rules cannot fully function within the Thai context. For instance, the concepts of fiduciary duties and derivative actions have not developed in Thailand as they have in common law jurisdictions due to the limited roles of the Thai court, the practices of the legal profession, and Thai civil procedure law. It is therefore questionable whether Thai agents can adopt common law rules into the Thai legal system in a workable way.

Scholars point out the significant role of local legal agents in shaping the adopted rules. Friedman mentioned that the legal professionals were those who handled ‘the technical job of importing or adapting foreign law, or, ... smoothing the process of moulding local law to suit new needs and new social desires’.⁴⁶ Berkowitz *et al* proposed that legal transplants were likely to be effective if the local agents were already familiar with the basic principles of foreign legal doctrines.⁴⁷ They play a significant role in applying the rules and adjusting them to the local context. Where the agent has a proper understanding, the adopted rules will be employed correctly and effectively.

It is argued that Thai legal agents may not be able to adopt a common law approach to the application of the rules because they are trained in civil law processes. Unlike the common law system where courts are bound by previous decisions – *stare decisis*, in theory in the civil law, a judge is not bound by previous cases but assumed to decide every case on the basis of the independent application of the statute.⁴⁸ The statutes made by the legislature are the law while the decisions are only a weaker and secondary

⁴⁶ Friedman, above n 12, 96.

⁴⁷ Daniel Berkowitz, Katharina Pistor and Jean-Francois Richard, 'The Transplant Effect' (2003) 51 *American Journal of Comparative Law* 163, 189.

⁴⁸ Max Rheinstein, 'Common Law and Civil Law: An Elementary Comparison' (1952–1953) 22 *Revista Juridica de la Universidad de Puerto Rico* 90, 96. However, it is argued that in civil law countries the judges in a lower court tends to follow a higher court decision especially when the line of former cases is clearly developed. This is because the judges in a lower court avoid having their decisions reversed by the higher court.

source of law. Common law, in the past, mainly created civil and commercial law through judicial decisions. Pejovic observed these historic differences:

A civil lawyer usually starts from a legal norm contained in a legislation, and by means of deduction makes conclusions regarding the actual case. On the other hand, a lawyer in common law starts with the actual case and compares it with the same or similar legal issues that have been dealt with by courts in previously decided cases, and from these relevant precedents the binding legal rule is determined by means of induction. A consequence of this fundamental difference between the two systems is that lawyers from the civil law countries tend to be more conceptual, while lawyers from the common law countries are considered to be more pragmatic.⁴⁹

Such differences between the common law and the civil law systems are blurring. In common law countries, judicial decisions are no longer the main source of law. In the US, during the 19th century, the states started codifying parts of the common law.⁵⁰ In company law there has also been attempts to have uniform company legislation. The Model Business Corporation Act was drafted for the state legislatures to enact in order to give greater certainty to corporate law.⁵¹ The purpose of commercial legislation in common law countries has been similar to that in civil law countries. In civil law countries, the concept of precedent is also evident. *Jurisprudence constante*, a body of consistent decisions by superior court, is not so different from *stare decisis* in the common law.⁵² To maintain social order and promote economic growth, legal stability and predictability are vital. Importantly, there is also justice in treating alike cases alike.

In addition to the similarity of the two legal systems, Thai legal agents are capable of implementing common law rules into the Thai legal system. Thai local agents therefore have a fundamental understanding of the rules from common law jurisdictions from which Thai company law has developed. At the level of legal training, a large number of Thai law students undertake their postgraduate study overseas, especially in English-

⁴⁹ Caslav Pejovic, 'Civil Law and Common Law: Two Different Paths Leading to the Same Goal' (2001) 32 *Victoria University of Wellington Law Review* 817, 820.

⁵⁰ See Arnald Kanning, 'Codification of the Common Law in the United States: An Economic Perspective' (TILEC Discussion Paper No DP 2004-009, Tilburg University, Tilburg Law and Economics Center, 2004).

⁵¹ Ibid 15.

⁵² Rheinstein, above n 48, 96.

speaking common law countries including the US and the UK. Although it is arguable that a one-year LLM program may not have as significant an effect on their legal reasoning as their primary legal education, they have an understanding of common law legal culture, methodology, and practices. In legal practice, because of international trade, Thai lawyers must deal with international clients, and advise on issues relating to common law. This extends the knowledge and experience of those who have graduated from common law jurisdictions. The internet also facilitates Thai judges and lawyers access to common law materials. Overall, although it is unlikely that Thai judges and lawyers, educated in civil law, will have a similar understanding, or common law mindset, as common lawyers do, there are factors both facilitating and encouraging Thai legal agents to educate themselves in common law principles.

8.4.3 Strengthening Thai corporate law and regulation

It has already been pointed out that, firstly, some German concepts and practices can be applied in the Thai legal system and, secondly, Thai legal agents are capable of understanding and applying rules derived from common law jurisdictions. A further issue to be considered is how to strengthen Thai corporate law and regulation.

As mentioned earlier, US companies are modelled on a system of outsider control. Market, legal and regulatory controls function together to provide a level of protection for minority shareholders. Given the concentrated ownership structure, there is little market control over Thai companies. Legal and regulatory controls are also weak. Unlike the courts in common law jurisdictions, the role of the Thai court in developing legal concepts or shaping the scope of duties of both directors and controlling shareholders is very limited. Neither public nor private enforcement plays a significant role in deterring mismanagement. The transplanted rules may not bring similar protection for minority shareholders as they do in the US in the absence of the same procedures in the legal system, or the same practice in the legal profession. Furthermore, compared with German practices, there is also no strong internal control seeking to balance the power of controlling shareholders with the interests of all stakeholders. Cooperation among managers, bankers, labour representatives or other

shareholders does not exist in the Thai context. In concentrated ownership companies, controlling shareholders have sufficient voting power to dominate a shareholders' meeting and appoint their associates to the board of directors. It is questionable how Thai law can protect minority shareholders when both internal and external control is weak.

8.4.3.1 Family-owned companies

Despite the concern about the power of controlling shareholders, in practice, controlling shareholders in Thai listed companies may not act against the company's interests due to their significant stake in the company. According to Claessens *et al*, there is a relationship between the use of pyramidal and cross-holding structures, and the risk of expropriation of minority shareholders by controlling shareholders.⁵³ Compared to other East Asian countries, the use of those financial structures in Thailand is less common.⁵⁴ The close ratio of cash flow to control rights in Thai companies reflects that Thai controlling shareholders are reluctant to extract significant private benefits as this affects their own stake in the company. Wiwattanakantang studied the economic performance of Thai firms and found that those with controlling shareholders performed relatively well due to the pyramidal structure being less used.⁵⁵ This finding accords with the opinions of legal practitioners and independent directors who were interviewed. Almost every one of those interviewees pointed out that, due to their large stake in the company, majority shareholders have a strong incentive to protect the company's interest. The connection between majority shareholders and the companies is not limited only to the capital they invest but also extends to the family's reputation. A corporate lawyer emphasised that it is the character of the Thai family and its members that is significant:

From my experience, majority shareholders feel that they are owners of the companies and do their best to protect the companies' interest because their stakes are large. Clearly larger than those of minority shareholders. Regarding the performance of

⁵³ See Stijn Claessens et al, 'Disentangling the Incentive and Entrenchment Effects of Large Shareholdings' (2002) 57(6) *The Journal of Finance* 2741.

⁵⁴ Stijn Claessens, Simeon Djankov and Larry HP Lang, 'Who Controls East Asian Corporations?' (Policy Research Working Paper No 2054, World Bank, 1999) Table 6.

⁵⁵ Yupana Wiwattanakantang, 'Controlling Shareholders and Corporate Value: Evidence from Thailand' (2001) 9 *Pacific-Basin Financial Journal* 323, 359.

family-owned companies, it depends on families and groups. Some groups are doing well; while, some are not. A Thai family business is similar to the Chinese one. The operation is quite systematic. Positions are clearly divided among family members. Younger generations are well trained and educated overseas. Success of a family business depends on, firstly, family members. If family members are concerned with the company's interest, the company will perform well. However, if they fight among themselves, the company's performance will be poor. Secondly, the rules governing the company, that is whether the family members are well controlled. From my view, a family business is normally successful as family members feel that they are owners of the business. They see the company not only as their investment channel but the family's assets which are shared among existing and future family members. Majority shareholders comply well with legal requirements, especially the related-party transaction requirements. In my opinion, a company with concentrated ownership performs better than a company with diffused ownership.⁵⁶

An investor confirmed this view of the families and their interest in the success of their firms:

A Thai business grows from a family business. As a result, family members and the founders' acquaintances are brought into the companies' management. Companies generally do business with other companies in the same groups. This fact is generally known. Investors are also aware of these facts and check information about companies before investing. To control these companies, the SEC stipulates the rules prohibiting related-party transactions and requires companies to disclose information. It is true that the level of minority shareholders' protection depends on the behaviour of majority shareholders – whether they are behaved well or not. From what I have seen, most directors of listed companies behave well. The explanation is that the majority shareholders have a large stake in their company and they want to maintain their wealth for the next generations. They therefore have a direct and strong incentive to protect the company's interest.⁵⁷

⁵⁶ Interview with a corporate lawyer, Bangkok.

⁵⁷ Interview with an investor, Bangkok.

A financial analyst further pointed to changes, resulting partly from changes in law, which had increased families' concerns about their reputation:

Majority shareholders can manipulate the companies in the way they want. It is a matter of fact that Thai companies are developed from family businesses. To expand these companies, large shareholders have to allow outsiders in but the company's policies are still initiated by the large shareholders. In the past, large shareholders totally ignored minority shareholders. For example, the general meeting took a very short time, for example 15 minutes; or the meeting was held in a location which made it impossible for minority shareholders to attend. Inevitably, a lot of people believe that the company's founder decided to list the company in the market just to take advantage of small investors. However that idea is no longer true. The change I have seen is the increasing numbers of rules which listed companies must follow. These rules raise the costs of compliance. Plus, listed companies are evaluated every year and the result of the evaluation is published. It is too burdensome to be listed companies just to take money from the public. As well, majority shareholders are more concerned about both their own investment and their reputation. Financial analyses and news reports assist shareholders in finding and digesting information. At the same time, financial analysts and news reporters function as watchdogs.⁵⁸

A professional independent director referred to contrasting styles of ownership and management in Thai listed companies.⁵⁹ She also saw benefits for a company in having a large shareholder:

People usually think that majority shareholders usually take advantage of minority ones, but this is not always true. In some cases, minority shareholders trust majority shareholders and they can work together very well and amicably. In terms of performance, it cannot be decided whether a company with single majority shareholders or a company with a lot of small shareholders performs better. In fact, performance depends on the companies' operation and fields of industry. Both types can perform well but with different styles of management. In the past, Thai business was generally family-owned. This is common for small capital markets. When the company gets bigger, the shareholding becomes diluted. As a result, shareholders have power to remove the former owners from the company's management. The turning point in the

⁵⁸ Interview with a financial analyst, Bangkok.

⁵⁹ Vallejo also argued that a family firm had a specific element of culture that helped it to survive through different family generations. Manuel Carlos Vallejo, 'Is the Culture of Family Firms Really Different? A Value-Based Model for Its Survival through Generations' (2007) 81 *Journal of Business Ethics* 261.

Thai capital market is the 1997 financial crisis. The crisis forced companies to find additional capital to revive and grow their businesses. In the case of [Siam Commercial Bank], the major shareholder is the Crown Property Bureau.⁶⁰ Its stake is high and, unlike other banks, the government cannot interfere. During the crisis, SCB planned to increase its capital and the financial advisor opined that the Crown Property Bureau should be the core shareholder and pledge to lead the operation but that it would not take advantage from the increase in capital. Given the strong reputation of the Crown Property Bureau, a large number of investors decided to invest with SCB. This consequently led SCB through the crisis. Shareholders, management and business are related. Business relies on shareholders and management. In a diffused ownership company, there is no major shareholder to convince other shareholders to remain with the company or to attract outside investors. Large shareholders are beneficial, especially in a long-term business as they make the company more stable and can be the leaders during times crisis.⁶¹

Similarly, Bebchuk *et al* evidenced the relationship between concentrated ownership and the limited appropriation of private benefits:

Since family pyramids and cross-holding structures tend to grow gradually through the generation of internal capital and the issuance of minority stock, one might expect family controllers to limit their appropriation of private benefits in order to assure continued growth for the benefit of their offspring.⁶²

8.4.3.2 Independent directors

From these findings it can be concluded that controlling shareholders add some value to the company, which is seen to directly benefit minority shareholders.⁶³ The problem

⁶⁰ Crown Property Bureau was established in 1936 to manage the Thai royal assets and properties. See *Background* (2011) The Crown Property Bureau <<http://www.crownproperty.or.th/home/main2.php?sec=eng>> at 20 March 2012.

⁶¹ Interview with a professional independent director, Bangkok.

⁶² Lucian Arye Bebchuk, Reinier Kraakman and George Triantis, 'Stock Pyramids, Cross-Ownership and Dual Class Equity: The Mechanisms and Agency Costs of Separating Control From Cash-Flow Rights' in Randall Morck (ed), *Concentrated Corporate Ownership* (2000) 306.

⁶³ Anderson and Reeb studied the S&P 500 and found that family firms perform better than non-family firms. They concluded that minority shareholders were not adversely affected by family ownership. Ronald C Anderson and David M Reeb, 'Founding-Family Ownership and Firm Performance: Evidence from the S&P 500' (2003) 58(3) *The Journal of Finance* 1301.

remains, how to ensure that controlling shareholders do not exploit the minority shareholders' interests?

As mentioned, in Thai corporate governance practices, there are no internal and external controls balancing the interest of all stakeholders and monitoring the management. The only balance to the controlling shareholders' power within the company is independent directors. One may argue that it is difficult to ensure that such directors will perform their duty independently and for the benefit of all stakeholders. Independent directors have a personal connection with the management and controlling shareholders and are reluctant to oppose them.⁶⁴ However, the interviews revealed that independent directors, to some degree, have influence over the management and can be relied on to protect the minority shareholders' interests.⁶⁵ In large Thai listed companies, independent directors are generally retired bureaucrats, legislators, members of the Council of State, and professors from leading universities.⁶⁶ These people tend to see themselves as professional independent directors. They are more concerned for their reputation than the personal connections between them and the management. They work effectively to ensure that a decision made by management is in the interests of the company. A legal practitioner pointed this out in an interview:

Independent directors are normally knowledgeable and highly qualified, such as retired government officials and former professors in leading universities. Officers from the military also hold positions in listed companies. A company benefits from these people in three ways. Firstly, the company can employ the connections which these people have. Secondly, these outside directors can provide some suggestions to the board; and, finally, having outside directors in the board can improve the company's image. It is important to state here that independent directors are not bad persons. They do not work only for the remuneration. In practice, independent directors assist the company in

⁶⁴ Piman Limpaphayom and Thomas J Connelly, *Corporate governance in Thailand* (2004) Thai Institute of Directors Association <<http://ssrn.com/abstract=965300>> at 20 March 2012, 40; see also Section 4.2.2.3.

⁶⁵ Dahya *et al* suggested that independent directors could increase the value of a concentrated ownership company. Jay Dahya, Orlin Dimitrov and John J McConnell, 'Does Board Independence Matter in Companies with a Controlling Shareholder?' (2009) 21(1) *Journal of Applied Corporate Finance* 67.

⁶⁶ For instance, the board of Bangkok Bank, one of the leading Thai banks, is composed of six independent directors. Those independent directors include a member of the Thai royal family, a former senator, a member of the Council of State, the Dean of Faculty of Commerce and Accountancy, a former Deputy Commanding General of Royal Thai Navy. See *Companies/Securities in Focus. BBL: Bangkok Bank Public Company Limited* (2012) The Stock Exchange of Thailand <<http://www.set.or.th/set/companyprofile.do?symbol=BBL>> at 20 March 2012.

creating mechanisms to supervise the company's operational system. They realise the scope of their duties and give careful advice to the board. They will do their best as independent directors because they do not want to ruin their reputations.⁶⁷

A corporate lawyer partly agreed with these opinions and also saw the law on directors' duties as having some influence on their behaviour:

In my opinion, it is common for large shareholders to appoint independent directors from their acquaintances. Large shareholders will only choose people they can get along with and who do not interrupt their corporate policies. Given their close relations, one may argue that these independent directors may work as rubber stamps. I believe that this is not always true. Firstly, the law clearly specifies the scope of directors and similar rules are applied to both managing and independent directors. Independent directors have to follow these rules and, if they do not, they might be sued. They have a good understanding of their duties. They will not risk themselves by approving any issues proposed by the management. Secondly, these independent directors are highly qualified and reputable. They have their own reputation and integrity to maintain.⁶⁸

A professional independent director expressed some irritation with minority shareholders in explaining the unappreciated role he undertook to protect their interests:

Minority shareholders sometimes assume that they are treated unfairly then become resistant. The source of all these problems is the minority shareholders' negative attitude towards majority shareholders. They believe that majority shareholders gain from the loss of the minority shareholders. They believe this because there have been a lot of news regarding unfairness in companies due to majority shareholders. Consequently, minority shareholders expect independent directors to be their representatives and protect them. That is not correct and can make [independent directors] feel uncomfortable. We work for the common interests of the company with sufficient consideration for minority shareholders but not as a representative of minority shareholders. People believe that we act like rubber stamps. I have to make this clear that we work together with the board, not against the board. If we oppose all the board's decision, it will be a deadlock in the management and this will affect everyone including minority shareholders. What we normally do is, when independent directors disagree with the management, we usually discuss ways to find amicable solutions

⁶⁷ Interview with an officer of the SEC, Bangkok.

⁶⁸ Interview with a corporate lawyer, Bangkok.

before the issues become public. This is to both resolve the problem and maintain the company's reputation.⁶⁹

Another independent director pointed to his role in diffusing conflicts by considering all interests:

Mostly, the management and independent directors cooperate well. Independent directors understand the business culture of the company. Holding a position on the board as an independent director is not simple. We must interact with all parties showing that we consider their interests. I think this is the key to being an independent director. We take the interests of all stakeholders into our consideration. In many cases, when two or more parties cannot agree on something, we play a role as a mediator to compromise the demands of all parties and resolve the conflict. Minority shareholders in particular rely on us heavily as they do not trust the management and controlling shareholders.⁷⁰

These views indicate that in the larger listed companies where independent directors have public reputations they may have positive effects on board decision making as it affects minority shareholders. The motives of the independent directors to speak well of their roles however should be noted. This evidence, however, suggests that it is an issue which needs to be further investigated.

Given the different historic local contexts it is unlikely that Thailand will adopt some German concepts, especially employees' participation. Nevertheless, Thailand may benefit from adopting some other German laws such as the use of electronic forums to facilitate communication among individual shareholders and the rules governing transactions between companies in the same group. Although transplanted rules from common law jurisdictions can succeed only to a limited extent, local legal agents are more familiar with common law concepts and have the capability to apply the transplanted rules. It is therefore more appropriate for Thailand to continue to adopt common law rules, particularly as they often are the source of international or transnational standards. In the absence of strong internal and external controls, minority

⁶⁹ Interview with a professional independent director, Bangkok.

⁷⁰ Interview with a professional independent director, Bangkok.

shareholders may rely, to some extent, on the large stake of controlling shareholders and the participation of independent directors to protect their interests.

8.5 Conclusion

In Thailand, legal transplants relating to the protection of minority shareholders are largely influenced by common law rules. However, the borrowed laws operate within a civil law system. The evidence reveals a series of legal transplants in Thai company law and shows that transplants are possible. While some adopted rules can be practically and successfully incorporated into the Thai context others cannot. The transplants that are mere procedures for a company to comply are easy to implement. On the other hand, due to different contexts, some of the adopted rules cannot function the way they do in the jurisdiction from which they are borrowed. This finding supports the thesis that law is culture-specific. The adopted rules on minority shareholders have generally developed to address the problems revealed agency theory. The conflicts of interests within Thai companies, on the contrary, lie not between shareholders and directors but between controlling and minority shareholders. Consequently, a number of adopted rules do not function in practice. Although German legal concepts, such as the supervisory board and labour co-determination may be an alternative model for Thailand to use to improve its protection of minority shareholders, due to their different backgrounds it is not possible for such concepts to be successfully transplanted into Thai law and practice. The evidence further suggests that, despite the differences in legal and social contexts, rules from common law jurisdictions can still be adopted to, and used in, the Thai legal system, as local agents are already familiar with common law principles and rules.

Chapter 9

Conclusions

- 9.1 Introduction
- 9.2 The background to the research
- 9.3 Conclusions to the research questions
 - 9.3.1 Does the Thai legal framework provide adequate protection for minority shareholders?
 - 9.3.2 Could the transplantation of the legal frameworks applied in other jurisdictions into Thailand be feasible?
 - 9.3.3 What are the obstacles to legal reform in Thailand?
- 9.4 Implications and research contribution
 - 9.4.1 Implications
 - 9.4.2 Research contribution
 - 9.4.2.1 Academic contribution
 - 9.4.2.2 Practical contribution
- 9.5 Limitations of the study
- 9.6 Suggestions for future research

9.1 Introduction

Thailand, as well as other emerging countries, has faced strong pressures to improve protection for minority shareholders in the past decade. It commenced with perceived needs to regain investors' confidence after the 1997 Asian currency crisis and to prevent a reoccurrence of corporate failures. Thailand has been strengthening its legal protection for minority shareholders by adopting legal concepts and practices from other jurisdictions. It is questionable whether many of the adopted rules are suitable for Thailand. The rules have mainly developed under the influence of agency theory in the legal systems from which they have been adopted to deal with the divergence of interests of the principals and agents, shareholders and managers. However, the conflict within Thai listed companies is between principals, controlling and minority shareholders. Furthermore, given the differences in the contexts between the donor and recipient jurisdictions, it is questionable whether the adopted rules can successfully be transplanted. These issues have been subject to only limited research. This research project, firstly, sought to map Thai laws and regulations and compare them with those

of United States and Germany. It then considered whether US and German laws and regulations could provide effective protection for minority shareholders in Thai companies in a Thai business context and how these laws may function in the Thai legal system. The key obstacles to legal reform in Thailand in this area have also been identified.

This chapter provides an overview of the conclusions drawn from the findings and analysis presented in the previous chapters. It then addresses the implications, as well as the limitations, of the study and concludes with suggestions for future research.

9.2 The background to the research

The thesis begins with an outline of the framework for the protection of minority shareholders in two jurisdictions – the US and Germany – and the region in which Thailand is located: East Asia. In US listed corporations share ownership is generally diffused amongst a large number of small shareholders. Given the small stake of each shareholder, control over the company has therefore shifted to the management. According to the literature, including Fama and Jensen, the fundamental problem is the divergence between the interests of management and those of the shareholders, known as the agency problem.¹ The managers may initiate and implement decisions that affect the residual claimants – the shareholders – without a direct interest in the assets they manage. They may act according to their self-interests rather than those of the shareholders. A number of mechanisms have sought to reduce this divergence and strengthen monitoring systems to better protect shareholder interests. These include aligning management and shareholder interests, having greater shareholding by blockholders, and appointing outsiders to the board of directors and forming of special committees. In addition, shareholders can rely on external mechanisms – the outside labour market and the market for corporate control – to replace slack management. These mechanisms have been developed on the assumption that minority shareholders have little power, or incentive, to monitor the management. This US model of good

¹ See Eugene F Fama and Michael Jensen, 'Separation of Ownership and Control' (1983) 26 *Journal of Law and Economics* 301; Eugene F Fama and Michael Jensen, 'Agency Problems and Residual Claims' (1983) 26 *Journal of Law and Economics* 327.

corporate law and governance has strongly influenced research in other jurisdictions and the model developed by the OECD and IMF amongst other international and transnational institutions.

German corporations, unlike the US model, are generally controlled by a limited numbers of families and banks. German companies have two boards – the management and the supervisory board. These two boards have their own authority but function together in the interests of the company and its stakeholders. The management board is overseen by three parties – the supervisory board, the banks, and controlling shareholders. The supervisory board has access to the same information as the management board and plays a role in overseeing the management. In large companies, employees' representatives make up half of the supervisory board. Under German business practice, German banks also have a direct interest in companies as shareholders, proxyholders, and lenders. The generally cooperative interaction between management, employees, banks, and controlling shareholders represents strong internal control over management.

East Asian listed corporations are different from the US and German models. The ownership of East Asian companies is generally very concentrated in the hands of limited numbers of wealthy families.² These families prefer investing in different activities rather than focusing on a core business. They organise their companies as part of a family business group. The owners control these companies through different ownership structures, including pyramidal and cross-holding patterns. Controlling shareholders have a direct influence over corporate operations and have significant incentive to prioritise their interests over the interests of the company and other shareholders. The mechanisms employed in the US, and propagated by international institutions, may not be suitable in East Asia. The protection employed in the US developed to control and regulate conflicts of interests between the shareholders and the management. However, the main problem in East Asia is the conflicts of interests

² Stijn Claessens, Simeon Djankov and Larry HP Lang, 'The Separation of Ownership and Control in East Asian Corporations' (2000) 58 *Journal of Financial Economics* 81.

between controlling and minority shareholders.³ Although there are similarities between East Asian companies and German companies, German corporate governance models may not function well in an East Asian context because of very different local circumstances, especially the absence of a strong history of labour participation. It is necessary to carefully assess whether, and how, Western models may be applied effectively in the East Asian context.

9.3 Conclusions to the research questions

From Chapters 4 to 8, the thesis examines the key concepts in minority shareholders' protection and maps the relevant legal issues in the three studied jurisdictions. This section concludes the analysis in those chapters which address the three research questions asked in this thesis.

9.3.1 Does the Thai legal framework provide adequate protection for minority shareholders?

Chapters 4 to 7 evaluate the sufficiency of the Thai legal framework on minority shareholders' protection. The US and German legal frameworks are used as the benchmarks. Legal protection is examined in four areas: the fundamental rights provided to minority shareholders; the fiduciary duties of directors and controlling shareholders; the protection provided in specific contexts; and, the remedies.

Two aspects of the fundamental legal rights of minority shareholders in US, German, and Thai law are compared: management and proprietary rights. The findings show that, in Thai law, there are appropriate allocations of rights for shareholders to participate in management and rights as share owners. For instance, minority shareholders receive timely information before a shareholders' meeting, and can vote by proxy. Listed companies are required to establish a nomination committee to recommend individuals qualified to be a board member to the shareholders' meetings and to have one-third of the board made up of independent directors. Thailand has recently adopted some other

³ Michael N Young et al, 'Corporate Governance in Emerging Economies: A Review of the Principal-Principal Perspective' (2008) 45(1) *Journal of Management Studies* 196.

principles which derive from US law, including shareholders' proposals and proxy solicitation. However, it is questionable whether such adopted rules will function in practice. For example, most Thai minority shareholders participate in the share market as speculators, not investors; they have no interest in putting shareholder proposals to a general meeting. Similarly, proxy solicitation is rarely used. Thai companies are generally controlled by large shareholders and it is generally impossible for minority shareholders to gain sufficient votes through proxies to overcome the controlling shareholders' power.

The laws and legal practices governing the fiduciary duties of the directors and controlling shareholders in these three jurisdictions are considered as their decisions directly affect minority shareholders. Interestingly, a convergence of the formal rules on the fiduciary duties of directors in the three jurisdictions is revealed. Directors are required to act in the best interests of the company and as a person in a similar position would. The concept of the business judgment rule, which was developed over a long time in English and US judicial practice, has been taken up in both German and Thai law. Despite the convergence, it is argued that the adoption of the US legal principle may not be successful in Thailand. In the US, the judges continue to craft legal statements of these fiduciary duties. However, in Thailand, the court has neither defined the scope or context of fiduciary duties nor recognised a business judgment rule because few cases are brought to it. Fiduciary duties therefore remain largely statements in the respective codes – as laws in the book. Without the participation of the judiciary to contextualise them to contemporary commercial practice, the statutory rules cannot further develop in an effective way in the Thai legal system. The duties of controlling shareholders have been acknowledged by US and German courts, but not by Thai courts. There are also no legislative provisions on the duty of controlling shareholders in Thai law. As no case has been brought by minority shareholders against controlling shareholders, the Thai courts have had no opportunity to consider this issue.

The study extends to how the laws and regulatory practices in the US, Germany, and Thailand protect minority shareholders in different situations, such as mergers, takeovers, and related-party transactions. It shows that, in statutory mergers and asset

acquisitions, Thai law provides more suitable protection to minority shareholders in a concentrated-ownership context than does US or German law. The companies to be merged must provide shareholders with a written opinion from independent financial experts. This is to ensure that shareholders can make decisions on an informed basis. To pass a resolution, a supermajority vote of the shareholders is also required. The research finds that proxy fights and hostile tender offers are very uncommon in Thailand and Germany compared with the US because of the concentration of share ownership in a limited number of shareholders. It is generally impossible to overcome the votes of existing shareholders. Despite the lack of hostile takeovers, Thai law has procedures to ensure that all shareholders can respond to proxy contests and takeover bids on an informed basis. The law further requires the board to send shareholders the advice of a financial expert to assist them in making a decision on whether to accept the offer. Directors may employ defensive mechanisms against a hostile bid only when approved by the shareholders' meeting. In freezeout transactions, Thai law does not allow the existing shareholders to cash out the equity interest of minority shareholders. The research suggests that Thai law should facilitate a shareholder who is likely to become the sole shareholder to acquire the rest of the company's shares. Regarding related-party transactions, the research shows that Thai law provides sufficient protection for minority shareholders because only disinterested shareholders can approve the relevant transactions.

In addition to outlining the rights and protection provided to minority shareholders, the remedies available to them are also examined. The research categorises the remedies into two: private and public. Minority shareholders in Thai companies can institute a derivative action against directors on behalf of the company. In practice, minority shareholders do not initiate such an action. This is because, firstly, the five per cent shareholding threshold imposed by the law is excessively high given the average amount of shares held by minority shareholders. Also, there is no easy, economic or timely mechanism to facilitate communication between minority shareholders or in coordinating their votes. Thirdly, as in other jurisdictions with derivative actions without a significant financial interest, minority shareholders are unlikely to initiate a legal action. This is also one reason why minority shareholders also do not take legal

actions to recover damages for personal losses they may have suffered. Also, unlike in the US and Germany, there is no form of class action, contingency fees and litigation funding are also not permitted in Thailand. Private enforcement in Thailand is seen to be significantly weak.

The role of securities regulators in public enforcement is analysed. It reveals that the role of the securities regulators in the three jurisdictions is significantly different. In Germany and Thailand, the supervisory authorities have a very limited range of powers in enforcing securities laws. This appears to be inconsistent with the widespread belief that state institutions in civil law jurisdictions are more powerful than those in common law jurisdictions. They have no authority to bring an action against wrongdoers to reimburse damaged investors. It is suggested that Thai law expand the powers of the Thai SEC as private enforcement does not function effectively. It should be entitled to order directors to desist from a potential wrongdoing and to bring a civil action for misconduct against directors to reimburse shareholders who have been harmed. However many Thai practitioners believe that the Thai securities regulator is not sufficiently competent or resourced to undertake such cases.

In all, the evidence suggests that Thai laws in the books provide sufficient fundamental rights to protect minority shareholders. Directors owe fiduciary duties to the company. In specific contexts, such as mergers, takeovers, and related-party transactions, Thai law requires the provision of an opinion from independent financial advisors to be submitted to minority shareholders before they vote. Minority shareholders are also empowered to bring an action against mismanagement on behalf of the company against directors. The research, however, reveals that some of the adopted rules are not used and capable of functioning in a Thai context.

9.3.2 Is the transplantation of the legal frameworks applied in other jurisdictions into Thailand feasible?

The answer to the first research question indicates that some of the adopted legal concepts are not functioning in the Thai legal environment. The research, therefore,

focuses on the feasibility of transplanting legal rules and concepts on minority shareholders' protection into the Thai legal system.

An examination of legal transplants into Thai company law establishes that, firstly, Thailand has largely adopted company law from common law sources; and, secondly, such transplants into Thai company law have proved possible. The main factor driving these legal transplants within Thailand has been the Thai political elite. Under political pressure in the late 19th and early 20th centuries, Thai rulers decided to change fundamental basic of the Thai legal system and reform it using a mix of French and German civil law models. Their motives were partly to restore Thai sovereignty by removing extraterritoriality and partly to facilitate economic growth. In that period, Thai legal agents, who also were the political elites, played an important role in facilitating the transplanting of the adopted rules. A large number of legal practitioners had studied in England and were familiar with the adopted rules of company law, although some lawyers did not entirely understood basic concepts such as separate legal personality. In present, many Thai legal practitioners have studied abroad and through that, and the internet, are familiar with common law principles. Company law may have been more easily transferred due to its loose connection with other social processes.

Although transplants are possible, the research further questions whether they are successful. Despite the fact that Thai legal agents are familiar with the adopted rules, other general rules and the entire legal system are based on civil law. According to Teubner, the adopted rules that have been operating in a context that is different from their origin may not produce the same results as they do in the system from which they are borrowed.⁴

The success of the transplantation of the rules on minority shareholders' protection is determined by whether the adopted rules can protect minority shareholders in Thai companies. There is evidence that some adopted rules have been successfully transplanted into the Thai business and legal context, while some other rules have not. The conclusion drawn is that the rules that have a loose connection with social

⁴ Gunther Teubner, 'Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences' (1998) 61 *Modern Law Review* 11, 12.

processes or other institutions in the donor and recipient systems have been comparably easier to transplant. This finding supports Teubner's argument that suggests a relationship between rules and social context.⁵ The rules that cannot be successfully transplanted include shareholders' proposals, derivative actions, and, the fiduciary duties of directors. This is, at least in part because these rules have been developed under the influence of agency theory. They developed to protect the interests of minority shareholders in a diffused ownership firm. On the other hand, Thai companies are concentrated in the hands of controlling shareholders. Furthermore, these rules are also tied into the professional practice of common law, such as contingency fees. The wide use of litigation in common law permits the judges to use discretion in their contextualisation of fiduciary law to particular cases. Some adopted rules, therefore, are not as applicable in the Thai context.

As the findings show that transplants of rules from common law jurisdictions are not always successful, further issues are raised. Firstly, whether, due to their similar legal heritage, Thailand will benefit from adapting German legal concepts to provide better minority shareholders' protection; and, secondly, whether Thailand should retain the law which has been adopted from common law jurisdictions.

The main features of German internal control are the supervisory board, the role of banks, and employees in co-determination. Despite a similar legal heritage and corporate structures, the adopting of this internal control system may not be possible as employee participation is not recognised in Thai law nor supported by Thai society. However, Thailand could still employ German legal principles regulating transactions between companies in the same group and the use of the electronic Federal Gazette to allow communication among individual investors.

In respect of whether Thailand should retain the law which has already been transplanted from common law system and continue transplanting laws from these jurisdictions. The findings show that, despite the difference between the legal systems, Thai legal agents are familiar with common law rules and are capable of applying them.

⁵ Ibid.

This is because a large number of them have graduated from institutions in common law jurisdictions. Also, working with foreign clients has encouraged them to educate themselves about common law. The research, however, points out that the adopted rules may not function in the way that they do in the US due to the different legal systems and the difference in local contexts. Derivative actions offer no incentive to minority shareholders to use them. As class actions, contingent legal fees and litigation funding are not allowed in Thailand, it is not possible to expect that shareholders will use the threat of litigation as a mean to monitor management. In the Thai capital market, external control mechanisms are absent. In term of enforcing law, it may be possible to rely on the self interest of controlling family shareholders with the participation of independent directors.

9.3.3 What are the obstacles to legal reform in Thailand?

Thailand has been reforming its corporate laws with a number of recent revisions and additions. These are intended to provide better protection to minority shareholders and, consequently, may bring some changes in Thai corporate governance practices. However, achieving successful legal reform is not an easy task. There may be resistance from people adversely affected by the reforms or within the Thai legal system itself. The research sought to key obstacles to legal reform by examining the Thai legal system, regulatory organisations, business practices, and culture. There requires further research. The apparent key obstacles to legal reform in Thailand are the failure of legal transplants; the absence of local demand for the legal reforms; and, ineffective enforcement.

In respect of the failure of some transplants, Thai legislators have aimed to reform the law to provide better protection. However, if the law cannot be implemented, there is unlikely to be no change in the legal and regulatory systems.

The 2008 Thai Securities and Exchange Act created a number of legal tools that attempt to strengthen minority shareholders rights and encourage them to exercise them. An examination found that some of them cannot function. Under the provisions for

shareholders' proposal, shareholders are allowed to initiate a shareholder proposal to communicate their opinions to management. The management may include the proposal as an agenda item at the shareholders' meeting. However, eligible shareholders must individually or collectively hold at least five per cent of the company's shares. This requirement filters out almost all minority shareholders. It is difficult for them to communicate with, or coordinate their activities with, other shareholders. Also given the nature of Thai small shareholders, they are speculators rather than long-term investors. Their concern is for the short-term return rather than the long term protection of the rights provided. Also in 2008 a provision on proxy solicitation was adapted to ensure that shareholders receive information before proxies are granted. Nevertheless, the proxy solicitation may not be applied in Thailand. Given the strong, concentrated ownership of Thai companies, it is not possible to gather sufficient votes from minority shareholders to install new directors.

In addition to the new rights provided, some other existing rules have not been successfully transplanted into Thai legal system. As mentioned, the Thai company was originally influenced by English law and more recently by US law. However, the legal context in which the adopted laws operate does not facilitate their effective functioning. A clear example is derivative actions. They are a legal mechanism that allows minority shareholders to bring a legal action against mismanagement. Active enforcement by this means may deter mismanagement and change corporate governance practices. In Thailand, however, no derivative action brought by minority shareholders in public companies has been heard in the Thai Supreme Court. This is because, unlike the US practice, contingent and conditional fees are not allowed in Thailand. Without the lawyers' participation, minority shareholders have no incentive to spend their time and money to initiate an action, as they have no direct financial interests in the damages which are reimbursed to the company. The absence of derivative actions partly reflects a wider apparent reluctance amongst Thai people to litigate. It partly reflects the small shareholdings which give no minority shareholders an interest in litigating. Derivative actions, though provided, cannot function in practice.

The other examples involve laws that require the court's interpretation to give guidance to their operation. It is not possible for legislators to draft a law that can apply to every potential case. It is therefore necessary to rely on the court to apply the law on a case-by-case basis. The area where judicial interpretation is required is the fiduciary duties of directors. The convergence of the rules on fiduciary duties in US, German, and Thai law has been pointed out. However, the application of these rules differs.⁶ In the US, the court plays a leading role in giving both scope and content to fiduciary duties. The decisions adjust the law to fit with business trends and public expectations. In Thai law, there are no precedents on the scope of fiduciary duties in Thai law. In the absence of a clear guidance, the legal profession may have difficulty in predicting the outcome of cases. Minority shareholders prefer to sell their shares rather than initiate litigation. Also in the absence of class actions and contingent fees, no shareholder is likely to spend time and money on such issues. Consequently, the Thai court has not had a chance to establish precedents on directors' duties.

The second obstacle is the lack of demand for legal reform and the resulting law. According to Berkowitz *et al*, transplants can be successful if the demand for law exists. The demand is necessary, as it will lead to the law in the books be using in practice. To match the demand, legal institutions work to develop the law. Furthermore the demand for law has the potential to provide sufficient resources to support the enforcement of law. The demand for legal reform in Thailand in this area appears to be relatively weak.

The strongest demand for law reform appears to have come from international and transnational institutions outside Thailand. The Thai political elites have accommodated their wishes in the reforms made. Within Thailand there appears to have been little demand for these changes or the resulting law. Small shareholders who are directly affected by corporate failure have shown little interest in the change. Both the corporate

⁶ Kanda and Milhaupt observed the characters of the courts in civil and common law systems:

While [the] difference in judicial mindset can be exaggerated, it is fair to say that at least historically, common law judges have been more comfortable than their civil law counterparts in working with open-ended standards.

Hideki Kanda and Curtis J Milhaupt, 'Re-examining Legal Transplants: The Director's Fiduciary Duty in Japanese Corporate Law' (Working Paper No 219, The Center for Law and Economic Studies, Columbia Law School, 2003) 15.

structure and minority shareholders' behaviour were analysed to obtain a clear picture. The data shows that the size of the Thai capital market is relatively smaller than that of some other comparable East Asian countries. Individual investors are reluctant to invest in the stock market because they have a limited understanding of securities trading and are afraid of losses. Retail investors are mainly speculators rather than long-term investors. After the 1997 financial crisis controlling shareholders had to dispose of some of their shares to maintain their core businesses but the control through their families remains strong. The next largest shareholders, foreign and domestic investors cannot overcome the power of the controlling shareholders. The large number of remaining small shareholders is short-term speculators. They have no incentive to pressure the government for better law or enforcement.

The third obstacle is the absence of effective enforcement. The role of the Thai government in initiating legal reform is apparent. After the 1997 financial crisis, it, together with the Thai market supervisory authorities, established several organisations to improve corporate governance, including the National Corporate Governance Committee, Director Responsibilities Steering Group, Corporate Governance Center, Thai Institute of Directors Association, and the Thai Investor Association. They all, together, may put pressure on company directors to comply with laws, regulations and codes. These organisations, nevertheless, take no part in enforcing the laws.

Both private and public enforcement in Thailand is significantly weak. Private enforcement plays no role in deterring mismanagement as minority shareholders rarely initiate cases against directors for the reasons already given. Although the laws on derivative action impose the costs of the plaintiff shareholders on the company, minority shareholders are still reluctant to initiate legal action. Two reasons relate to derivative actions in all jurisdictions. The plaintiff shareholders receive no direct benefit as the amount recovered goes to the company, which remains under the same directors. Public enforcement is also not strong. Prosecutors hardly ever win securities cases. The Thai SEC has no authority to initiate a civil action against wrongdoers. Neither it nor the enforcement authorities practice the plea bargaining used by the US SEC and Department of Justice in criminal prosecution in corporate and securities cases in the

US. Consequently, there is no evident success in punishing wrong doing to defer companies and directors. Without enforcement, the rules will exist only in the books.⁷

In conclusion, although there have been extensive attempts to improve laws and regulations on minority shareholders, legal reform in Thailand has not always be successful. The lack of success is because of, firstly, the mismatch between the introduced laws and the legal system. The adopted rules may provide the best protection for minority shareholders but if they cannot be transplanted into the Thai legal system no change is going to happen. Secondly, there has been no strong demand from those who are affected by corporate fraud and small investors to pressure the government to pay more attention to Thai corporate law and regulatory practices. Political pressure may lead to reform in this area. Finally, without effective enforcement there is no deterrent to mismanagement and no reimbursement of minority shareholders' losses.

9.4 Implications and research contribution

9.4.1 Implications

Thailand, like many jurisdictions with a developing economy, has attempted to improve its law regulatory practices to meet international standards. However, the standards, principles, or rules that can function in one jurisdiction may not function in others. The research findings tend to support the view that legal transplantation is less likely to be successful when the rules are connected to affiliated social process. The rules that develop in a specific environment may not survive in the recipient jurisdiction with its different social and political environments. It is therefore important for Thai law and policy makers to have a more complete understanding of the adopted rules and whether they can function in practice. Importantly, more consideration needs to be given to modifying any adopted rules in order to make them fit with the local Thai context.

⁷ This evidence supports North's theory which suggests that a borrowed law to be effective there had to be, in the recipient legal system, compatible dispute resolution, debt enforcement, and bankruptcy procedure. Douglass C North, *New Institutional Economics and Third World Development* (1995) 17–27.

The findings reveal that overall Thai law provides sufficient rights and protection to minority shareholders. Thailand may choose to adopt some US or German legal concepts to provide additional protection. To strengthen Thai legal practices, Thailand should pay more attention to legal enforcement. Legal enforcement institutions – the market regulator, the securities regulation investigating authority, and, public prosecutors – exist. The courts and the legal professions also exist and permit litigations to be used to enforce shareholder rights. They need to function collaboratively to enforce the law. Again the research has pointed out that shareholders' litigation in the US is supported by the use of class actions, contingency and condition fees for legal professions, litigation funding, and plea bargaining. They are not used in Thai law. Attempts to introduce them may be resisted and, if they were to be, careful consideration of them would be needed to ensure that their impact did not have negative consequences.

Together with public enforcement, private enforcement cannot be ignored. It is necessary to consider how to encourage shareholders to monitor the management and facilitate them to initiate a civil action.

The findings also show that legal agents are the key to both law enforcement and the implementation of borrowed law, especially in the case of the adoption of rules from different legal systems. It is necessary to ensure that legal agents have an understanding of the adopted principles. The Thai government should encourage legal educational institutions to provide opportunities for legal practitioners and law students to learn how these principles have been developed in the jurisdictions from which they come and research on how such rules may function in the Thai legal system. This is to assist Thai legal practitioners develop an understanding of the origin of the adopted rules. The reports and other background documents used by policy and law makers in enacting the adopted principles should be accessible. They will provide Thai legal practitioners with a more complete picture on whether the adopted principles are intended to operate in similar or different ways compared with their origin, and importantly, why the rules are enacted as such. The Thai government can also learn from the legal practitioners' experience. Their feedback on the adopted rules can be used in future legal reform.

The analysis of the cultural, economic and legal factors relating to Thai corporate law and governance and results of the empirical study suggest that there are alternative mechanisms to improve corporate governance. In a jurisdiction where external control – the market for corporate control and regulatory enforcement – is weak, the findings suggest a greater reliance on controlling shareholders to protect minority shareholders. It is argued that in concentrated ownership companies controlling shareholders are a source of the conflict as they usually ignore the interests of the company and all other shareholders. However, the findings provide an interesting contradiction. The relationship between cash flow and control rights reflects the separation between ownership and control of a company.⁸ Through pyramid and cross-shareholding structures, the ultimate voting power of controlling shareholders is higher than the number of shares they actually hold.⁹ Compared with other East Asian countries, controlling shareholders in Thai companies rarely use pyramid or cross-shareholding structures.¹⁰ This is reflected in the reduced gap between control and cash flow rights in Thai companies. Controlling shareholders tend to have strong incentives to protect the interests of the company as they have a direct financial interest in it. They see the company as not only their investment but a family business important in maintaining the wealth of future generations. These findings suggest that minority shareholders benefit from having large shareholders in the company. Nonetheless, this can lead to related-party transactions that siphon wealth from the company as a whole to controlling shareholders. Law and regulatory practices should ensure that the transactions between companies in the same group are transparent and approved by disinterested shareholders.

Given their power in the company, controlling shareholders may also abuse their power by appointing incompetent directors to the board. This will frustrate the role of independent directors in overseeing the company and ensuring that the board performs its functions. Given the close connection between independent directors and the controlling shareholders, independent directors may not act independently. The

⁸ Claessens, Djankov and Lang, above n 2, 109.

⁹ Stijn Claessens et al, 'Expropriation of minority shareholders: Evidence from East Asia' (Policy Research Working Paper No 2088, World Bank, 1999) Table 1.

¹⁰ Ibid Table 4.

findings, however, reveal that professional independent directors are knowledgeable, highly qualified, and well known. They are concerned to protect their reputation and integrity. This suggests that Thailand could build up a pool of professional independent directors providing a wide range of qualified directors to listed companies. The initial steps towards setting this up have been taken by the Thai Institute of Directors Association. There should be ongoing educational or training support for directors in the pool. Strong and professional independent directors may improve corporate governance at the firm level.

9.4.2 Research contribution

9.4.2.1 Academic contribution

The major contribution to academic knowledge is in the understanding of law and regulation in the protection of minority shareholders in Thailand. The analysis of the legal sources, secondary literature, and the field research will contribute to existing empirical studies and theoretical debates on a number of academic issues which have emerged, including the debate over whether law matters in economic development, proposed by La Porta *et al.*¹¹ Their law matters thesis suggests a strong relationship between common law institution and economic development. They claim that common law is predominant because, compared to civil law, it can provide better protection to investors. It is implied that to better develop sound and stable financial markets, emerging countries should harmonise their laws with the law of common law jurisdictions. On the other hand, recent research conducted by Milhaupt and Pistor leads to a different conclusion.¹² They studied the relationship between law and economic development in the US, Germany, Japan, South Korea, China, and Russia and found that there is no one type of legal system uniquely associated with economic success.¹³ They have found a rolling relationship between law and economic growth. Emerging

¹¹ See Rafael La Porta et al, 'Law and Finance' (1998) 106(6) *Journal of Political Economy* 1113; Rafael La Porta et al, 'Investor Protection and Corporate Governance' (2000) 58 *The Journal of Financial Economics* 3; Rafael La Porta et al, 'Investor Protection and Corporate Valuation' (2002) 57 *The Journal of Finance* 1147.

¹² Curtis J Milhaupt and Katharina Pistor, *Law and Capitalism: What Corporate Crises Reveal about Legal Systems and Economic Development Around the World* (2008).

¹³ *Ibid* 220.

countries may expect that standardisation will improve the quality of their legal system and institutions. While legal harmonisation is easy to achieve, the legal rules, concepts or doctrines do not function in a vacuum.¹⁴ They are interdependent. It is unlikely that a legal concept incorporated into a system can function in conflict with other legal rules as processes. In addition, the legal agents who apply the borrowed rules should have an understanding of the basic concepts behind the rules.¹⁵

The findings in this thesis are significant in the law matters debate. In respect of corporate law, Thai law is a hybrid. The basic legal system is civil law however since before the reception of the civil law system Thai company had been adopted from English law. The findings are consistent with the work of Milhaupt and Pistor. It is found that although some legal concepts from common law jurisdictions have been incorporated into the Thai legal system, the adopted rules cannot provide as effective protection to minority shareholders as they do in the donor jurisdictions. The main reason is the difference between the local circumstances of donor and recipient jurisdictions. The adoption of derivative actions provides a clear example. In theory, this concept enables minority shareholders to bring an action on behalf of a company to recover damages for mismanagement. However, in practice, without the support of the legal professions and the rules relating to its fees derivative actions are unlikely to be used.

The research also contributes to the study of legal transplants. Thailand, similarly to other emerging countries, has sought to improve its legal system by employing legal principles from other jurisdictions. This research suggests that such legal transplantation is not a simple task. The findings indicate that although some transplanted rules have been incorporated into Thai law for some time, they have not been developed due to the difference between the local circumstances of the donor and recipient jurisdictions. This is consistent with Teubner's observation that the rules that tightly connect with social process are comparably difficult to transplant.¹⁶ The study reveals that both the US and German legal systems are distinctive. Thailand has adopted some of the US legal

¹⁴ Ibid 216.

¹⁵ Ibid.

¹⁶ Teubner, above n 4, 12.

concepts such as shareholders' proposals and proxy solicitation but, without similar legal concepts and institutions, the adopted concepts cannot function as they do in the US legal system. Besides, due to the different social, historical, and legal background, even though some of the German legal concepts, such as co-determination or a supervisory board may benefit Thailand, they are not suitable for the Thai local context.

The study particularly focuses on law and regulation in the Thai local context. Although there have been several studies on the protection of minority shareholders in Thailand, they consider this issue only as part of wider studies of corporate governance. The existing studies have not sufficiently considered Thai business and legal culture. This research provides a more detailed study of minority shareholders' protection and examines the key elements required for their more effective protection. In addition, the interviews with legal practitioners, independent directors, regulators, academic researchers, and legal enforcement agencies provide a better understanding of the application of those principles in the context of Thai business and legal culture. The research considers the gaps between the formal rules and the behaviour of the participants in corporate governance and indicates the actual outcomes of the transplantation of these principles into Thai law and regulatory practices. As a result the missing elements that are required for more effective protection of minority shareholders and the obstacles to their development and enforcement in Thailand are revealed.

9.4.2.2 Practical contribution

The research makes a contribution to understanding the development of law and policy in Thailand on minority shareholders' protection. This will benefit future law reform in Thailand. The research indicates that Thai law provides sufficient protection to minority shareholders and that it is necessary to focus on implementing the law. Firstly, it is important to understand that adopting US models or international standards into formal statements of the law does not guarantee economic success. Secondly, Thai law reformers have to realise that law reform is not limited to a process of copying formal law. The research also suggests that Thailand must shape its own model. Consideration

of the practicality of the adopted rules must be considered. As the rules on minority shareholders' protection interconnect with other rules, their reform without acknowledgement of their effect on other parts of the legal system, and the effect of those parts of the legal system on them cannot be successful. As suggested by Pistor, 'isolated change of some provisions in corporate law can have at best little impact on the overall direction of the evolution of corporate law'.¹⁷ To enhance enforcement of the law and the participation of minority shareholders, reforms of relevant legal institutions are required. Importantly, legal agents who apply and adopt the rules must have sufficient knowledge of the borrowed rules. Changes to legal education for legal practitioners are required as well as education and training other participants in the background and potential use of the rules. This needs to be supplemented with better and more available official commentaries and law reports.¹⁸

The study is also relevant to the development of legal and regulatory frameworks, and their implementation, in other emerging economies. To set up an effective system of minority shareholders' protection there are many issues for these emerging countries to consider. These include the possible outcome of legal transplantation, the implementation of adopted rules, and domestic obstacles to their acceptance and enforcement. Similarly to other studies, the research indicates that no one system or standard of corporate governance is most effective in promoting economic growth. It is therefore important to consider whether the principles applied in developed countries are able to solve the problems of these emerging countries. The formal rules may not function well in practice. This study provides a case study for emerging countries on issues to consider the design of an effective legal model to protect minority shareholders. It is also relevant to understanding the limitations on the use of legal and regulatory transplants in developing jurisdictions.

¹⁷ Katharina Pistor et al, 'Evolution of Corporate Law: A Cross Country Comparison' (2002) 23 *University of Pennsylvania Journal of International Economic Law* 791, 864.

¹⁸ Roderick A Macdonald and Hoi Kong, 'Patchwork Law Reform: Your Idea is Good in Practice, but It Won't Work in Theory' (2006) 44 *Osgoode Hall Law Journal* 11, 52.

9.5 Limitations of the study

The research compares laws and regulations in three jurisdictions – the US, Germany, and Thailand. Given the diversity of US state laws, Delaware corporate law was selected for the study given its significance for major US companies and US company law generally.¹⁹ It is therefore not possible to make generalisations about US state company law. It is also affected by US federal law and securities regulation. The range of German literature on corporate law and governance was limited as the researcher does not speak or read German. Although there is significant literature available in English, the findings may have been different if a broader range of German literature had been read. An important limitation is the lack of comparison with other East Asian legal systems' protection of minority shareholders. This was dictated by the resources available for this project but remains a significant issue for further investigation. In addition, there is limited literature on legal transplants in the Thai legal system. Also, there has been limited research into the roles of interest groups in advocating for and resisting transplants. Had more detailed studies been available, the findings on legal transplants in respect of minority shareholders' protection may have been different.

The research methodology was designed to achieve a complete understanding of Thai business and corporate practices as could be achieved in research on this scale. The selected interviewees were chosen from a wide range of interest groups and people with experience in corporate law and regulation. The professionals were selected on the basis of their reputation for wide experience and were assumed to be representative of their occupational groups. Individual interviewees expressed their opinions regarding the questions asked based on their own personal experience. The findings, therefore, may not be employed to represent the viewpoints of the organisations to which they belong nor to make assumptions about the views of their occupations or interest groups. Additionally, due to time limitations, interviews were conducted only in the Bangkok region. These limitations may also affect the findings although Bangkok is the

¹⁹ The website of Delaware's Division of Corporations recites that '[m]ore than 850,000 business entities have their legal home in Delaware, including more than 50% of all US publicly traded companies and 63 % of the Fortune 500'. *Division of Corporations* (2011) State of Delaware <<http://www.corp.delaware.gov/>> at 20 March 2012.

commercial capital. The findings may have been different if a broader range of interviews had been conducted in other regions.

The legal framework of minority shareholders' protection in listed companies in general is considered. There is no differentiation between listed companies. The research may have led to different findings should the characteristics of each company, for example, their industry sector, market, capitalisation size, or ownership structure have been taken into consideration.

9.6 Suggestions for future research

The findings of this study point to several opportunities for future opportunities. Firstly, similar research may be conducted with more interviewee samples to provide additional understanding of Thai business and corporate culture and obtain more viewpoints of those affected and legal practitioners, including judges in particular, on legal transplants in Thailand.

Secondly, future research could address some of the limitations of the study identified. For example, as the study does not consider differences between listed companies, it would be desirable to explore specific industry sectors, size of market capitalisation, ownership structures and the members of generations which have controlled large family companies.

Thirdly, future research may expand the results of the study. Recommendations have been made suggesting the desirability of educating Thai legal practitioners and building up a pool of professional independent directors. Future research may include: a greater focus on an understanding of Thai legal culture, agents and institutions. It may also include a greater investigation of the role of independent directors which, from this research, appears to be equivocal. This could extend to the process for training and encouraging them to perform their duties independently and effectively.

Finally, future research may investigate how other Asian countries incorporate rules into their legal systems; how to independently develop legal solutions to improve corporate governance; and, how they prepare their legal agents and institutions to implement these new rules. There are a number of civil law countries that have experienced substantial reforms, particularly in adopting Anglo-American corporate and securities laws, and Thailand may be able to learn from their own individual experiences.

INTERVIEW SCHEDULE

Part I: Concepts

1. What does minority shareholders' protection mean to you? Why is it important?
2. Companies have a number of important issues to deal with such as corporate strategy and competitiveness, public relation, corporate integrity, corporate governance, etc. Of the top 10 issues where do you think they rank minority shareholders' protection? Why?
3. Would the controllers of Thai listed companies, in your experience, generally see minority shareholders' protection as being as important as you do?
4. The Thai Securities and Exchange Commission (SEC), the Thai Stock Exchange, and Thai Rating and Information Service (TRIS) have conducted several surveys evaluating the quality of corporate governance in Thai listed companies; how seriously do these companies consider the results of such surveys? (Prompt: Of the top 100 companies listed in the Thai stock exchange less than 50 companies have participated in these surveys, why don't they all participate? When a company takes part in a survey, is there any pressure on other companies in the same industry to participate?)
5. In your view, how well are minority shareholders protected in Thai listed companies?
6. Apart from any legal requirements, do Thai listed companies provide any additional rights to minority shareholders? If they do, what are the incentives for them to do so?
7. It is well known that Thai listed companies are in the hands of a few families. How do you see this affecting minority shareholders' protection in these companies? (Prompt: management, compensation, related party transactions)

Appendix A

Part II: The Roles of Related Participants

8. After the financial crisis in 1997, the ownership structures of some Thai listed companies changed significantly.

(a) In some companies, the shareholdings of controlling shareholders were diluted; with new shareholders gaining 10%-25% of the companies' shares and becoming the 2nd or 3rd largest shareholders, how have these new shareholders affected the management of these companies? (Prompt: have these new shareholders made a difference to minority shareholders?)

(b) Institutional investors came to control some companies; how has this affected the management of these companies? (Prompt: have institutional investors made a difference to minority shareholders?)

(c) Foreign investors gained significant shareholdings in some companies; how has this affected the management of these companies? (Prompt: have foreign directors made a difference to minority shareholders?)

9. Generally speaking, gatekeepers such as credit rating agencies, accountants, and lawyers, have a duty to monitor whether the law has been contravened; what role do you see them playing in protecting minority shareholders?

10. When minority shareholders complain to directors about breaches of the law or questionable practices and decisions, how do the directors respond?

11. Independent directors are considered to have as core functions the balancing of the benefits for controlling and minority shareholders and also monitoring the directors' activities. How effective do you think these directors are in protecting minority shareholders?

Appendix A

Part III: Regulations and Development

12. In your opinion, is it proper and necessary for the government to intervene in the market to protect minority shareholders? If so, how far should the government do so? (Prompt: does the global financial crisis justify more intervention?)

13. Thailand has adopted laws from different countries and international organisations in its corporate and securities laws which reflect western standards. Do you think employing such standards is suitable in Thailand? Will the global financial crisis lead to hesitation or resistance to observing these standards? (Prompt: independent directors?, disclosure requirements?, and board sub-committees?)

14. Do you think that adopting some of the following principles from other developed countries will advance the rights of minority shareholders in Thai listed companies?

- supervisory boards.
- civil penalties.
- oppression remedies.
- whistle-blower protection.

(Prompt: How well would these principles fit into the Thai legal and regulatory system?)

15. In your view what are the critical obstacles to improving the protection of minority shareholders in Thailand? (Prompts: political opposition?, fit with Thai laws and regulatory practice?, and the connection between families and political parties?)

16. The latest Securities Act has imposed several more duties on directors, company secretaries, and auditors. What effect do you see the Act having on them?

Appendix A

Part IV: Law Enforcement and Remedies

17. Are criminal prosecutions against corporate wrongdoers in Thailand effective? If not, how could they be made more effective?
18. Minority shareholders in Thailand rarely bring civil actions. How do you explain this?
19. In developed countries such the US and the UK, regulatory agencies play important roles in protecting minority shareholders when the law is breached; for instance, the Australian Securities and Investments Commission is entitled to bring a civil action against wrongdoers; however, the Thai SEC is not allowed to do so. Do you think empowering the Thai SEC in this way is necessary? If so, are there any limitations which should be imposed on its intervention?
20. The derivative action has been introduced into Thai security law. Do you think it will offer effective protection to minority shareholders?
21. The latest Securities Act has introduced the principle of the business judgment rule. How do you think the courts will interpret and apply this concept? How far will the courts exercise their authority to protect minority shareholders?
22. Do you think the Thai legal system is effective in supporting minority shareholders' protection? Do you think that Thai judges and lawyers are sufficiently knowledgeable and experienced to provide better protection to minority shareholders?
22. In Hong Kong, a 'shareholders support fund' and the establishment of a shareholder activist group to protect interests of minority shareholders has been suggested. Do you think such a scheme would be effective in Thailand or advance minority shareholders' rights? (Prompt: Do you think that, in Thailand, it would be possible to have a Non-Government Organisation protecting or acting on behalf of minority shareholders?)



INFORMATION TO PARTICIPANTS INVOLVED IN RESEARCH

You are invited to participate

You are invited to participate in a research project entitled "A Legal Framework on Promoting Minority Shareholders' Protection in Thailand".

This project is being conducted by a student researcher, Nilubol Lertnuwat, as part of a PhD study at Victoria University under the supervision of Professor Neil Andrews from the Faculty of Business and Law.

Project explanation

The purpose of the research project being undertaken is to assess the effectiveness of the legal framework for minority shareholders' protection in Thailand, to assess the impact of international standards on minority shareholders' protection in Thai listed companies, as well as the difficulties in achieving better protection for minority shareholders in Thailand.

What will I be asked to do?

You are invited to participate in an interview which takes about one hour. The interview is about your opinions on minority shareholders' protection in Thai listed companies. It relates to both legal and regulatory practices. It seeks to draw on your experiences with these. You are, however, not obliged to disclose anything which you are not comfortable with or answer any question which you do not wish to.

What will I gain from participating?

Your comments, based on your knowledge and experience, will contribute to possible solutions to problems in the protection of minority shareholders in Thailand. It will lead to a better understanding of Thai corporate governance and regulatory practices and may lead to improvements in both of them.

How will the information I give be used?

The information you provide will be contained in a thesis which will be available in the library of Victoria University. Also some parts of the information may be published in various academic journals. Your response to questions will remain confidential. You will not be named as having participated in the research project/Your identity will be kept strictly confidential. Your statements

Appendix B

or comments may be republished in the thesis or the articles, but not in such a way that you, and your organisation, could be identified.

What are the potential risks of participating in this project?

Minimum risks have been identified from participating in this research. Throughout the interview, if you feel uncomfortable or require some form of explanation, please feel free to raise the issue with the researcher. As indicated, you are free not to answer any question. However, you will not be identified as the maker or author of any statement. Also, the statement or comment will not be used in a way which will enable you to be identified. You may withdraw at any time and for any reason without prejudice.

How will this project be conducted?

To make recommendations on how to establish an effective legal framework for minority shareholders in Thai listed companies, it is necessary to study some selected aspects of minority shareholders' protection. Collection of data for this study will involve two distinct sources. The first source is literature on minority shareholders' protection in developed jurisdictions including Australia, the United States, and the European Union, and the recommendations made by international organisations. The second source is interviews with people experienced with Thai corporate governance and legal and regulatory practices including professional independent directors, corporate lawyers, auditors, non-governmental organisations, and other public institutions working on minority shareholders' protection.

Who is conducting the study?

This project is conducted by

Professor Neil Andrews (Neil.Andrews@vu.edu.au) and

Ms Nilubol Lertnuwat (Nilubol.Lertnuwat@live.vu.edu.au)

Any queries about your participation in this project may be directed to the Principal Researcher listed above.

If you have any queries or complaints about the way you have been treated, you may contact the Secretary, Victoria University Human Research Ethics Committee, Victoria University, PO Box 14428, Melbourne, VIC, 8001 phone (03) 9919 4781.



CONSENT FORM FOR PARTICIPANTS INVOLVED IN RESEARCH

INFORMATION TO PARTICIPANTS:

We would like to invite you to be a part of a study, "A Legal Framework on Promoting Minority Shareholders' Protection in Thailand", to determine suitable legal standards and practices for the Thai legal and regulatory framework on the protection of minority shareholders.

CERTIFICATION BY SUBJECT

I, _____

of _____

certify that I am at least 18 years old* and that I am voluntarily giving my consent to participate in the study: "A Legal Framework on Promoting Minority Shareholders' Protection in Thailand" being conducted at Victoria University by Professor Neil Andrews.

I certify that the objectives of the study, together with any risks and safeguards associated with the procedures listed hereunder to be carried out in the research, have been fully explained to me by Ms Nilubol Lertnuwat

and that I freely consent to participation involving the below mentioned procedures:

- an interview: (please choose an appropriate box)
 - ☐ in which the answer will be recorded on an audio tape, or
 - ☐ in which the answer will be recorded in the form of note taking.

I certify that I have had the opportunity to have any questions answered and that I understand that I can withdraw from this study at any time and that this withdrawal will not jeopardise me in any way.

I have been informed that the information I provide will be kept confidential.

Signed:

Date:

Any queries about your participation in this project may be directed to the researcher Professor Neil Andrews at +61 (0)3 9919 1826 or Neil.Andrews@vu.edu.au.

If you have any queries or complaints about the way you have been treated, you may contact the Secretary, Victoria University Human Research Ethics Committee, Victoria University, PO Box 14428, Melbourne, VIC, 8001 phone +61 (0)3 9919 4781

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