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## Corporate Governance Rules under Argentine Law

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# CORPORATE GOVERNANCE RULES UNDER ARGENTINE LAW

*Rodrigo Olivares Caminal\**

## I. INTRODUCTION: AN APPROACH TO CORPORATE GOVERNANCE - GENERAL APPLICABLE RULES<sup>1</sup>

IN popular usage, *corporate governance* refers to the role of the board of directors, shareholder voting, proxy rights, and other transactions taken by the shareholders to influence corporate decisions.<sup>2</sup> One key element in improving economic efficiency is corporate governance.<sup>3</sup> Basically, it is the system by which companies are directed and controlled.<sup>4</sup> Moreover, good practice in corporate governance requires commitment, professionalism, and above all ethical behavior.<sup>5</sup> It is clear that corporate governance is not an end in itself,<sup>6</sup> but it can be considered the path to benefit shareholders and to serve the public interest in general.

A clear example of the importance of corporate governance is drawn

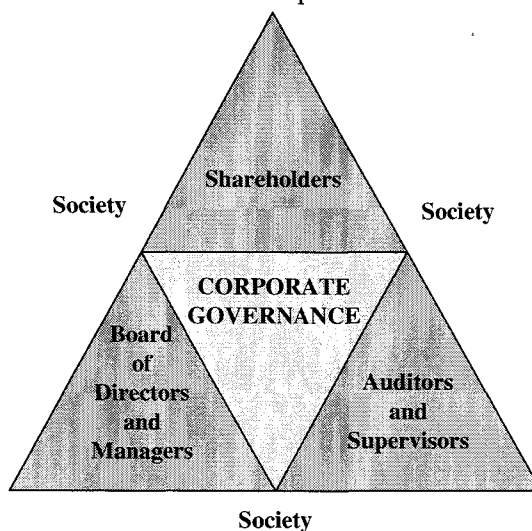
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1. El Derecho or "ED," La Ley or "LL," and Jurisprudencia Argentina or "JA" are three different collections of case law, comments on judgements and articles in Argentina. These publications have two ways to be quoted: (i) by date, because they are published as a newsletter on a daily basis (e.g., ED, March 24, 1973) or (ii) by volumes, after being published the newsletters are compiled in different volumes (e.g., L.L. 155-597, which means La Ley, Volume 155, page 597). Note that La Ley has changed the way of numbering the volumes. Rather than following subsequent numbering, they are numbered by year and letters (e.g., LL, 1987-D-346, which means La Ley, Year 1987, Volume D, page 346). In addition, "CNCom." is the acronym of the Commercial Court of Appeals of the City Buenos Aires, the main court of commercial matters in Argentina. It is divided into five rooms of three judges each, designated A, B, C, D, and E. Lastly, "CSJN" is the acronym for the Federal Supreme Court of Justice of Argentina.
2. RICHARD A. BREALEY & STEWART C. MYERS, *PRINCIPLES OF CORPORATE FINANCE* 976 (6th Int'l ed. 2000).
3. *OECD Principles of Corporate Governance*, ORG. FOR ECON. CO-OPERATION & DEV., at 11 (1999), available at <http://www.oecd.org> (last visited Mar. 21, 2003) [hereinafter *OECD*].
4. A. CADBURY, *CORPORATE GOVERNANCE: BRUSSELS, INSTITUUT VOOR BESTUUNDERS* (1996).
5. LUTGART A.A. VAN DEN BERGHE & LIESBETH DE RIDDER, *INTERNATIONAL STANDARDIZATION OF GOOD CORPORATE GOVERNANCE: BEST PRACTICES FOR THE BOARD OF DIRECTORS* 5 (1999).
6. *Where were the Directors? Guidelines for Improved Corporate Governance in Canada*, TORONTO STOCK EXCHANGE COMMITTEE ON CORPORATE GOVERNANCE IN CANADA (1994).

up from research done by McKinsey & Company<sup>7</sup> where: “an overwhelming majority of investors are prepared to pay a premium for companies exhibiting a high governance standard. Premiums averaged 12-14% in North America and Western Europe; 20-25% in Asia and Latin America; and over 30% in Eastern Europe and Africa.”

Corporate governance could be graphed as a triangle, formed by three smaller triangles representing: (i) the shareholders and stakeholders; (ii) the board of directors and managers; and (iii) the auditors and supervisors’ inter-relationship. After the Enron crisis and the enactment of the Sarbanes-Oxley Act,<sup>8</sup> the latter has received much preponderance. These interactions of the three triangles create a fourth triangle in the middle that reflects the corporate governance. This would not be completed, however, unless its relation with third parties is considered (i.e., society).



In Argentina, there are three primary sources of law and regulation relating to corporate governance: (1) the Companies Law Number 19,550 as amended and restated (ACL); (2) the Securities Law Number 17,811 (SL); and (3) regulations issued and enforced there under by the Superintendency of Corporations (*Inspeccion General de Justicia* or IGJ)<sup>9</sup> and the National Securities Commission (*Comisión Nacional de Valores* or CNV).<sup>10</sup>

7. McKinsey & Co., *Global Investor Survey 2002: Key Findings* (July 2002), at <http://www.mckinsey.com>.

8. The Sarbanes-Oxley Act was passed by the United States Congress on July 25, 2002.

9. The Superintendency of Corporations is Argentina’s controlling authority on companies, which depends on the Ministry of Justice as per Law No. 23.315, art. 1.

10. The CNV is an autarkic entity with jurisdiction covering the territory of the Argentine Republic. The CNV was created by the Public Offerings Law No. 17.811. Its main purpose is to ensure the accuracy of Argentina’s securities markets, to watch over the market price formation process, and to protect investors. The CNV supervises corporations authorized to issue securities to the public, the secondary markets where these securities are traded, and all persons and corporations in-

In 2001, the Argentine Government introduced a major reform to the regulatory framework applicable to the public offer regime. The reform incorporated the Corporate Governance Principles of the Best Practices Code of the Organization for Economic Co-Operation and Development (Corporate Governance Principles), which were not already incorporated in the Argentine legal system. Decree 677/01 (Transparency Decree or TD), which became effective on June 1, 2001, introduced such amendments and implemented the so-called Public Offering Transparency Regime.

The Organization for Economic Co-Operation and Development (OECD) created policies by a convention signed in Paris on December 14, 1960. The OECD adheres to three goals. The first goal is to achieve the highest sustainable economic growth and employment, and a rising standard of living in member countries<sup>11</sup> while maintaining financial stability, and thus to contribute to the development of the world economy. The second goal is to contribute to sound economic expansion in member, as well as non-member countries,<sup>12</sup> in the process of economic development. The third goal is to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations.

The Corporate Governance Principles of the OECD can be summarized as: (i) rights of the shareholders; (ii) equitable treatment of shareholders; (iii) role of stakeholders; (iv) disclosure and transparency of corporations; and (v) responsibilities of the board.<sup>13</sup> The Corporate Governance Principles are intended to assist member and non-member governments in their efforts to evaluate and improve the legal, institutional, and regulatory framework for corporate governance in their countries. In addition, the Corporate Governance Principles provide guidance and suggestions for stock exchanges, investors, corporations, and other parties that have a role in the process of developing good corporate governance. Lastly, the Corporate Governance Principles focus on publicly traded companies.

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involved in any capacity in the public offering and trading of these securities. Public offering and trading of futures and options contracts is also under CNV jurisdiction, as are the related futures exchanges, clearing houses, and brokers intermediaries. See *Comisión Nacional de Valores*, available at <http://www.cnv.gov.ar/English/Main.htm> (last visited Mar. 18, 2003).

11. The original member countries of the OECD are Austria, Belgium, Canada, Denmark, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. Other countries that have joined the OECD include: Japan (1964), Finland (1969), Australia (1971), New Zealand (1973), Mexico (1994), the Czech Republic (1995), Hungary, Poland, and Korea (1996). See OECD, *Member Countries*, at <http://www.oecd.org> (last visited Mar. 18, 2003).
12. Argentina is not an OECD member. See *id.*
13. See OECD, *supra* note 4 (including the principles of corporate governance and their annotations).

The intention of this article is to analyze the Argentine legal system, including its incorporation and application of Corporate Governance Principles.

## II. STRUCTURE OF ARGENTINE CORPORATE ENTITIES

The ACL set the rules for the incorporation and performance for the following corporate legal entities: (i) *Sociedad Colectiva*; (ii) *Sociedad en Comandita Simple*; (iii) *Sociedad de Capital e Industria*; (iv) Limited Liability Partnership (*Sociedad de Responsabilidad Limitada* or *SRL*); (v) Corporation (*Sociedad Anónima* or *SA*); (vi) Corporation with a governmental major shareholding; and (vii) *Sociedad en Comandita por Acciones*.

In Argentina, the Corporation is the most important corporate form and is the legal entity generally used to do business.<sup>14</sup> Consequently, a broad legal framework has been developed and a large amount of judicial precedents and administrative resolutions have been passed interpreting rules or establishing certain applicable principles. Therefore, this comment will focus its analysis of corporate governance rules in Argentina from the perspective of the Corporation. This notwithstanding, corporate governance aspects are not limited to the large quoted companies.<sup>15</sup>

The corporation may be incorporated by two or more shareholders, which may be either national or foreign corporate entities<sup>16</sup> or individuals. Equity is divided into shares and each shareholder limits its potential liability to the value of the subscribed shares. Additionally, corporations are administered by a board of directors.<sup>17</sup> One or more statutory supervisors appointed at the shareholders' meeting shall be in charge of supervising the company. Under section 299 of the ACL,<sup>18</sup> except in respect of paragraph 2 thereof (when the corporate capital exceeds Argentine Pesos

14. See A. Enrique, *SRL, Un Vehículo Poco Utilizado*, 1995 E.D. 1017 (2002); see also *Suplemento de la Inspección General de Justicia* 1, L.L. (2000).

15. O. PASTRE, *GOUVERNEMENT D'ENTREPRISE: LES DIX COMMANDMENTS* (1996).

16. Likewise, it is important to note that foreign corporations can perform activities in Argentina through the establishment of a branch office (Law No. 19.550, art. 118), or can participate as shareholders in domestic companies (for which they must comply with the requirement of registration with the IGJ in accordance with Law No. 19.500, art. 123).

17. Although there are some countries that have a two-tier board of directors that separate the members as executive and non-executives (the first of them being the "management board" and the latter the "supervisory board"), in Argentina there only exists a "unitary" board that brings together the executive and non-executive board members. Under Argentine law, the duty of supervision shall be exercised by all the directors and shareholders. Besides this *per se* duty, a special supervisor or committee can be appointed.

18. In addition to being subject to internal control efforts, corporations shall be subject to control by the respective authority within their jurisdiction while they are doing business, at the time of their dissolution and liquidation, and in any of the following situations:

- (i) when they offer shares and debentures to the public;
- (ii) when their capital exceeds twenty one billion Australs (Note: as of Jan. 1, 1992, this figure is understood to be 2,100,000 pesos, see sections 1, 2 of Decree No. 2128/91 published in the Official Gazette on Oct. 10,

\$2,100,000), the appointment of the statutory supervisors is mandatory and shall be comprised by an odd number of members.

In accordance with the by-laws of the corporation, a vigilance committee comprised of three to fifteen shareholders may be appointed at the shareholders' meeting. The duties of this committee are very similar to those of the statutory supervisor. Because the adoption of a vigilance committee is not mandatory, corporations have not generally adopted such a committee. *Honoris brevatis*, we will not refer to the vigilance committee in this article.

As a general rule, companies making a public offering of their shares shall create an audit committee comprised of three or more members of the board of directors,<sup>19</sup> the majority of which shall be independent<sup>20</sup> pursuant to the criteria established by the CNV.

### III. SHAREHOLDERS' MEETINGS, LIABILITY, RIGHTS, AND EQUITABLE TREATMENT

#### A. SHAREHOLDERS' MEETINGS

Shareholders' meetings must take place at the company's legal domicile (registered office) or within the jurisdiction of its legal domicile,<sup>21</sup> and are either ordinary (*Asamblea Ordinaria*) or extraordinary (*Asamblea Extraordinaria*).

Ordinary meetings must be called at least once a year, within four months from the end of the fiscal year.<sup>22</sup> The meetings consider two major categories.<sup>23</sup> The first category includes financial statements, statements of income, distribution of earnings, board of directors' and statutory supervisors' reports, and any other measure relative to the corporate business upon which the ordinary shareholders' meeting is competent to render a decision in accordance to the law or by-laws or other

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1991), the amount may be updated by the Executive Branch whenever it deems necessary;

- (iii) when they are mixed-economy companies or when they are corporations with a major governmental shareholding;
- (iv) when they engage in capitalization or savings operations or in any manner borrow money or securities from the public with the promise of future services or benefits;
- (v) when they work public concessions or services; and
- (vi) when it is a company controlling or controlled by another subject to supervision pursuant to one of the above-referenced provisions.

Law No. 19.550, art. 299.

19. Decree No. 677/01 § 15.

20. The director shall be independent with regard to the company as well as to the controlling shareholders, and shall not perform executive functions in the company.

21. Law No. 19.550, art. 233.

22. See notice (*circular*) no. 69, May 15, 1973 (whereby the IGJ (formerly in that date *Inspección General de Personas Jurídicas*) settled the interpretation regarding the timing to summon the shareholders meetings to consider the financial statements. The first announcement or notice should be published in the Official Gazette and/or in a leading newspaper within four months from the end of the fiscal year).

23. Law No. 19.550, art. 235.

issues submitted by the board of directors. The second category includes the appointment and removal of directors and statutory supervisors, and performance and liabilities of same.<sup>24</sup> Ordinary meetings may also be called at any moment to consider any increase in authorized capital up to five times the original amount if it is authorized by its by-laws,<sup>25</sup> and other matters not delegated to extraordinary meetings.

Apart from the matters previously identified, the ordinary meeting in listed companies shall decide the following: (i) the disposition or encumbrance of all or a substantial part of the assets of the company when it is not carried out in the ordinary course of the company's business; and (ii) entering into the company's administration or management agreements.<sup>26</sup>

The extraordinary shareholders' meeting deals with all matters that are outside the competence of the ordinary shareholders' meeting; and amendments to the by-laws. In particular, the meetings hear the following: (i) the capital increase, except in the case of its authorized increase up to five times (it may only delegate to the board of directors the power to fix the time of issue and form and terms of payment); (ii) the reduction and repayment of capital; (iii) the redemption, reimbursement, and amortization of shares; (iv) the merger, transformation, and dissolution of the company; (v) the appointment, removal, and remuneration of the liquidators; (vi) the split-up of the company; (vii) the consideration of the accounts and other matters relating to actions taken by the liquidators in the company's winding-up that require a final resolution of approval; (viii) the limitation or suspension of the pre-emptive right for the subscription of new shares;<sup>27</sup> (ix) the issuance of debentures and their conversion into shares; and (x) the issuance of bonds.

Ordinary and extraordinary meetings are held when called by the directors or statutory supervisors or by shareholders representing at least a 5 percent of authorized capital, unless the by-laws permit a smaller number.

Notices of meetings are given by means of announcements or notices published for five days in the Official Gazette, at least ten days in advance of the date specified for the holding of meeting.<sup>28</sup> In addition, corporations referred to in section 299 of the ACL,<sup>29</sup> should publish the following information in one of the leading newspapers in Argentina: the

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24. J. M. FARINA, *COMPENDIO DE LAS SOCIEDADES COMERCIALES*, 345 (1989).

25. Law No. 19.550, art. 188. Note that although this capital increase has to be registered, it does not imply a reform to the by-laws. CNCom [152-D] L.L. 455 (1973); CNCom [155-A] L.L. 400 (1974); CNCom [155-C] L.L. 597 (1974).

26. Law No. 17.811, § 72.

27. It should comply with the requirements set forth in ACL art. 197. Namely, that: (i) the matter be included on the Agenda, and (ii) the shares in question are to be paid by contributions in kind or given in payment of previously existing obligations. Law No. 19.550, art. 197.

28. The "5-day publishing term" of the Official Gazette should be counted as business working days, while the ten-days in advance of the shareholders' meeting are counted in a row.

29. See *supra* note 18.

nature of the shareholders' meeting;<sup>30</sup> the date, time and place of the meeting;<sup>31</sup> the agenda, and the special requirements demanded by the by-laws for the attendance of shareholders. However, no publications are necessary when all shareholders are present and decisions are made unanimously.<sup>32</sup> Moreover, if the required quorum is not available at a meeting on first call, notice for a meeting on second call, which must be held within thirty days of the date for which the first meeting was called, must be given at least eight days before the date of the second meeting. The by-laws may authorize both meetings (on first and second call) to be convened by means of the same notice.<sup>33</sup> In the latter case, if the meetings are convened for the same day, it must be held within an interval of not less than one hour.<sup>34</sup> Listed companies shall publish notice of a meeting at least twenty days in advance, but not before forty-five days from the date of the meeting. These terms shall be computed as from the last publication.

Twenty days before the date established for the meeting, the board of directors shall place at the shareholders' disposal, in the main office or through electronic means, all the relevant information with regard to the meeting to be held, the documents to be considered therein, and the board of directors' proposals.

Up to five days before the date established for the ordinary meeting where the documents of the fiscal year shall be considered, the shareholders representing at least 2 percent of the corporate capital may deliver to the main office comments or proposals related to the company's business corresponding to the fiscal year.<sup>35</sup> The board of directors shall inform the shareholders that said comments or proposals are in the main office or that they may be consulted through electronic means.

Shareholders may be represented at any meeting by proxy.<sup>36</sup> A judge, a public notary, or a bank official must certify signatures of the granting parties on the proxies. In the event that the proxy has been issued in a foreign country, a notary public must certify the signature as to the identity and capacity of the signer, and as to his faculties to grant a power of attorney on his behalf or on behalf of the grantor company. The document should then be legalized following the procedure established by the

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30. IGJ's Administrative unpublished decision, Apr. 26, 1973.

31. "Laboratorios Bago S.A." CNCom. [1983-B] L.L. 745.

32. See I. Winizky, paper submitted in the 1st National Congress of Companies Law, LA CUMBRE (Aug. 1977); E. H. Richard & C. Brizuela, paper submitted in the 1st National Congress of Companies Law, LA CUMBRE (Aug. 1977); JUAN M. FARINA, TRATADO DE SOCIEDADES COMERCIALES 181 (1980); see also "Malacari, Bruno c/ Rodríguez, Amadeo," CNCom. Room D, July 28, 1976, unpublished.

33. See FERNANDO HORACIO MASCHERONI, ASAMBLEA EN LA SOCIEDAD ANÓNIMA 35 (1987).

34. Law No. 19.550, art. 237.

35. Law No. 17.811, art. 71.

36. Law No. 19.550, arts. 56, 239. IGJ Resolution No. 6/80. See MIGUEL A. SASOT BETES, LAS ASAMBLEAS 193 (1981); ZALDIVAR ET AL., CUADERNOS DE DERECHO SOCIETARIO PART 2, Vol. 2, Macchi 362 (1979); A. V. VERÓN, TRATADO DE SOCIEDADES COMERCIALES, VOL. III 709 (1993).



Hague Convention on the Abolition of Legalization of Documents of October 5, 1961, or at the nearest Argentine Consulate if the country where the document was signed has not ratified said convention. Nevertheless, directors, managers, statutory supervisors, and employees of the company may not represent shareholders.

To attend shareholders' meetings, shareholders must deposit their company shares or a certificate of deposit or records of non-certificated shares, issued for that purpose by a bank, securities account or other authorized institution for registration in the ledger of attendance at shareholders' meetings book no less than three business days prior to the fixed date.<sup>37</sup> The company will give them due vouchers of receipt, which will serve for admission to the shareholders' meeting.<sup>38</sup>

The ordinary shareholders' meeting at the first call requires the presence of shareholders representing the majority of the voting shares.<sup>39</sup> At the second call, the shareholders' meeting is considered in order irrespective of the number of shares present. In both cases, resolutions will be taken by an absolute majority of votes present that may be issued on the respective decision,<sup>40</sup> except when the by-laws demand a greater number.

The extraordinary shareholders' meeting shall meet at the first call with the presence of shareholders representing 60 percent of the shares entitled to vote, if the by-laws do not require a greater quorum. The attendance of shareholders representing 30 percent of shares entitled to vote is required for the second call, unless the by-laws fix a greater or lesser quorum. Resolutions in both cases shall be taken by the absolute majority of votes present that may be cast on the respective decision, except when the by-laws demand a greater number.<sup>41</sup>

In the following cases, the extraordinary shareholders' meeting resolutions shall be adopted by the favorable vote of the majority of shares entitled to vote: (i) the transformation, extension or renewal of the incorporation term, except for companies making public offers or quoting their shares on the stock exchange; (ii) the company's anticipated dissolution; (iii) the transfer of domicile abroad; and (iv) a fundamental change of the corporate purpose and total or partial repayment of capital. This provision shall be applied to decide upon mergers and split-ups, except with regard to the surviving corporation, which shall be ruled by regulations governing capital increase.<sup>42</sup>

## B. SHAREHOLDERS' LIABILITY

As a matter of principle, shareholders of local corporations enjoy the benefit of limited liability because the company is a legal entity indepen-

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37. FARINA, *supra* note 32, at 351.

38. See VERÓN, *supra* note 36, at 909.

39. J. O. ZUNINO, *RÉGIMEN DE SOCIEDADES COMERCIALES* 231 (1993).

40. FARINA, *supra* note 32, at 351.

41. Law No. 19.550, art. 244.

42. *Id.*

dent from its shareholders. A shareholder of a corporation is only liable for the obligations incurred by the corporation to the extent of the shareholders' subscribed capital.<sup>43</sup> Such principle is subject to certain exceptions. The ACL and the Bankruptcy Law Number 24,522, as amended and restated (ABL), describe certain scenarios under which shareholders may be held unlimited and jointly and severally liable for damages caused to, by or through the company.

### 1. *Unlawful Activities*

When a company having a lawful purpose carries out unlawful activities, it shall be dissolved and liquidated upon the petition of any party or on the initiative of the IGJ. The shareholders, directors, and supervisors shall be held unlimitedly and jointly and severally liable for the company's liabilities and the inflicted damages.<sup>44</sup> They shall also lose their right to any residual claim because any outstanding balance or asset of the corporation will become property of the Argentine Government. Those partners who evidence their good faith shall be excluded from these provisions.

### 2. *"Disregard of Legal Entity" Doctrine*

Section 54 of the ACL provides that shareholders of a local corporation or those who effectively control it shall be held unlimitedly and jointly and severally liable if such corporation has been used as a mere vehicle to pursue goals alien to the corporate purpose, breach the law or the *public order* or to impair third parties rights.

The majority of legal authors are of the opinion that for purposes of applying the *disregard of legal entity* doctrine it is necessary that the intention (or gross negligence) to inflict damages or breach the law be clearly evidenced. Recently, a Labor Court of Appeals has applied the doctrine in cases of breach of social security and tax regulations by means of hiring or keeping unregistered personnel.<sup>45</sup> We do not agree with this criterion<sup>46</sup> since it is clear that it is a breach of duty of the directors *in lieu* of the shareholders (if it cannot be proved that the shareholders have been aware of the unfulfillment) as the court has established.

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43. Shareholders with partially paid subscribed shares are required to pay the outstanding balance within two years from the date of subscription.

44. Law No. 19.550, art. 19.

45. "Delgadillo Linares," CNTrab. Room III, unpublished, Sept. 11, 1997; "Duquelsy," CNTrab. Room III, 1999-B, LL, Feb. 19, 1998.

46. In the same line of thinking, see Francisco Junyent Bas, *Responsabilidad de los Administradores Societarios por Fraude Laboral*, in REVISTA DE DERECHO PRIVADO Y COMUNITARIO 183 (2000); Germán Luis Ferrer, *La Responsabilidad de los Directores de Sociedades Anónimas y la Inoponibilidad de la Persona Jurídica en la Relación de Empleo "en Negro,"* in REVISTA DE DERECHO PRIVADO Y COMUNITARIO 203-40 (2000).

### 3. *Willful Misconduct, Negligence or Diversion of Assets*

Damage suffered by a corporation due to fraud or negligence<sup>47</sup> by partners or by controlling non-partners renders those responsible jointly and severally liable for the compensation thereof, without being entitled to offset such compensation with the profits that their action may have produced in other business dealings. This liability shall also extend to those shareholders that were aware of the other shareholders actions and failed to take proper actions to prevent the infliction of damage, even if they did not participate directly in the scheme. In this case, they shall be held liable on grounds of omission. A partner or controlling party who applies funds or assets of the corporation to its own use or business or that of a third party, is obliged to deliver the resulting profits to the corporation, and shall bear the losses at his sole expense.

### 4. *Voided Shareholders' Resolutions and Conflict of Interest*

Those shareholders who voted for the resolutions that are subsequently voided because there were illegal (in a broad sense) and caused damages, and the relevant shareholders acted either with negligence or willful misconduct shall be held jointly and severally liable for all damages arising from such resolutions, without prejudice to the liability of the directors and statutory supervisors.<sup>48</sup> Moreover, any shareholder with interests in conflict with those of the company has a duty to abstain from voting on any matter that relates to such conflict.<sup>49</sup> Breach of this provision may give rise to liability for damages when, without the vote of the party affected with the conflict of interest, the relevant resolution could not have been validly approved.

### 5. *Extension of Bankruptcy*

A first approach to the extension of a bankruptcy proceeding to a third party requires emphasizing that as a matter of fact it is not granted *per se*; hence it is only granted restrictively by the courts. This does not mean that extension of bankruptcy is never declared. However, in order for the declaration to be made by the intervening judge, a number of requirements that are detailed below have to be met.

Upon the request of the trustee or another creditor within the term specified by the ABL, the court may render a judgment whereby the bankruptcy proceeding is extended to another person (Person Subject to Bankruptcy) in the event that any of the following situations occurs:

- (i) Under the appearance of acting for the benefit of the ankrupt entity,<sup>50</sup> such Person Subject to Bankruptcy has performed acts in its

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47. As per section 902 of the Argentine Civil Code, the higher the level of care and prudence that must be kept, the greater the obligations derived from the potential consequences of the facts.

48. Law No. 19.550, art. 254.

49. *Id.* art. 248.

50. Assuming it is declared bankrupt.

own interest and managed the assets of such entity as if such assets were its property, thereby defrauding its creditors (acting in the personal interest of the Person Subject to Bankruptcy).<sup>51</sup>

- (ii) The Person Subject to Bankruptcy, which controls the bankrupt entity, has managed the business thereof to achieve aims alien to its corporate purpose, directing the bankrupt entity under a unified management in the interest of the controlling party or the economic group to which it belongs (abusing the control of the bankrupt entity).<sup>52</sup> The Person Subject to Bankruptcy would be the bankrupt entity's controlling party if: (a) it is determined that it directly or indirectly holds an interest, of any nature, in the bankrupt entity that provides the votes necessary to control the corporate decisions thereof; or (b) each of the persons that, acting jointly, have any interest (as described in (a) above), and are liable for the conduct detailed in (i) above.
- (iii) The assets and liabilities of the Person Subject to Bankruptcy and those of the bankrupt entity may not be distinguished (commingling of funds).<sup>53</sup>

The requirements provided in (i) above would be the following: (1) the pre-existence of a bankruptcy; (2) the determination that another Person (whether the bankrupt entity's shareholders, directors, managers, etc., or a controlling company of the bankrupt entity, in fact, the "owners of the business") act as if they acted on behalf of and for the benefit of the bankrupt entity; (3) such Person Subject to Bankruptcy transfers the bankrupt entity's assets as the Person Subject to Bankruptcy's assets and in its own interest; and (4) fraud to the creditors in general.<sup>54</sup> Therefore, mere ruinous mismanagement by the bankrupt entity's managers would not suffice.

### C. SHAREHOLDERS' RIGHTS AND EQUITABLE TREATMENT

Shareholders enjoy certain rights regardless of their participation in the capital stock of the company. In section II.C.1, we will describe broadly all the rights pertaining to all shareholders. In the subsequent part, section II.C.2, we will describe the rights pertaining to the shareholders in accordance to their different shareholding percentages as specified.

#### 1. *Rights Pertaining to all Shareholders*

- **Voting Rights:**<sup>55</sup> The first and most important right with which

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51. Law No. 24.522, art. 161(1).

52. *Id.* art. 161(2).

53. *Id.* art. 161(3).

54. See S. FASSI & M. GEBHARDT, *CONCURSOS Y QUIEBRAS* 374 (6th ed. 1997). See also RIVERA ET AL., *CONCURSOS Y QUIEBRAS - LEY 24.522* (1995); A. N. ROULION, *RÉGIMEN DE CONCURSOS Y QUIEBRAS - LEY 24.522* (1995).

55. This right arises from article 216 of the ACL, whereby each share entitles a shareholder to one vote. Law No. 19.550, art. 216.

shareholders are entitled is their voting right to decide on different matters at ordinary and extraordinary shareholder meetings.

- **Cumulative Voting:**<sup>56</sup> Shareholders have the right to elect up to one-third of the vacancies to be filled on the board of directors by the cumulative voting system.<sup>57</sup> The by-laws may not repeal this right nor regulate it in such a way as to hamper its exercise, but it is excluded in the event that the election takes place within different classes of shareholders. The board of directors may not be renewed partially or in stages, if this should prevent exercise of the cumulative voting system.
- **Right to be informed in Advance of the Matters to be discussed in the Shareholders' Meetings:**<sup>58</sup> All the matters to be discussed in the shareholders' meetings must be included in the agenda of the meeting previously published. All decisions on matters other than those

56. *Id.* art. 263.

57. The following procedure shall be followed:

- (i) The shareholder(s) who wish to vote cumulatively must notify the company within three business days before the date of the meeting.
- (ii) The company must inform the shareholder(s) who request concerning notices received. Without detriment thereto, the president of the shareholders' meeting must inform shareholders present that they are all entitled to vote cumulatively, whether or not they have served the notice.
- (iii) Before voting, the number of votes pertaining to each shareholder present shall be made known publicly and in detail.
- (iv) Each shareholder who votes cumulatively shall have a number of votes equal to the result of multiplying those he would have normally had by the number of directors to be elected. He may distribute them or accumulate them among a number of candidates not in excess of one-third of the vacancies to be filled.
- (v) Shareholders who vote by the ordinary or multiple system and those that vote cumulatively shall compete in the election of one-third of the vacancies to be filled; the ordinary or multiple voting system being applied to the remaining two-thirds. Shareholders who do not vote cumulatively will do so for all the vacancies to be filled giving each of the candidates the aggregate votes corresponding to them according to their shares entitled to vote.
- (vi) No shareholder may vote (dividing his shares for that purpose) in part cumulatively and in part in the ordinary or multiple system.
- (vii) All shareholders may vary the voting procedure or system before casting their vote, including those who notified their intention to vote cumulatively and fulfilled the requirements for that purpose.
- (viii) The result of the voting shall be counted per person. Those candidates voted by the ordinary or multiple system will only be considered elected if they receive the absolute majority of votes present; those candidates voted cumulatively and obtain a number of votes exceeding those obtained by the ordinary system, until a third of the vacancies is filled.
- (ix) In the event of a tie between two or more candidates voted by the same system, a further vote shall be taken in which only the shareholders that opted for that system shall participate. In the event of a tie between candidates voted cumulatively, the shareholders who, under the system, have already obtained the election of the candidates that they proposed shall not vote in the second election.

Law No. 19.550, art. 263.

58. Law No. 19.550, art. 236.

included on the agenda are null and void, except: (i) when the entire capital is present and decisions are adopted unanimously by the shareholders having the right to vote;<sup>59</sup> (ii) the appointment of those who are to sign the minutes; and (iii) when the case the shareholders decide to file a judicial claim for liability against directors when it is a direct consequence of a matter already included in the agenda.

- **Withdrawal Right:**<sup>60</sup> Shareholders who dissent with any of the following decisions may withdraw from the company and be reimbursed the value of their shares: (i) the extension of the duration term of the company; (ii) the change of the legal domicile to a foreign country; (iii) the fundamental change of corporate purpose; (iv) the total or partial recapitalization which involve a disbursement by the shareholders; (v) the merger or split-up when the shares received in exchange would not be listed; (vi) voluntary delisting of the shares of the company or withdrawal from public offering regime; or (vii) the change of form of organization of the company (*transformación societaria*, e.g., if a corporation transforms into a limited liability partnership). Shares shall be reimbursed at the value stated in the most recent balance sheet drawn up or that should be drawn up in compliance with legal provisions or regulations.

Shareholders of companies that offer their shares to the public or are authorized to have them quoted on the stock exchange may not exercise the right of withdrawal in the event of a merger or split-up, if the shares that they are to receive as a result of such merger or split-up are authorized to be offered to the public or quoted on the stock exchange. They may exercise such right if registration under those systems is withdrawn or rejected.

The right of withdrawal may only be exercised by those shareholders present at the meeting who voted against the resolution within the fifth day of such vote, and by those absent shareholders who evidence their standing as such at the date of the meeting, within fifteen days after it has been held. In such situations, the term shall be counted from the time when the company announces the withdrawal or rejection by notices published for three days in the Official Gazette and in one of the Argentine leading newspapers.

- **Right to Declare Void Decisions Adopted by Shareholders' Meetings:** Any decision by a shareholders' meeting that violates the law, regulations or by-laws may be challenged as being null by the shareholders who did not vote in favor of the respective decision and by those absent who prove their capacity as shareholders at the date of the decision in question.<sup>61</sup> Shareholders who voted in favor may object if their vote is voidable because of defects of will. It may also be challenged by directors, statutory supervisors, members of the vigi-

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59. *Id.* art. 246.

60. *Id.* art. 245.

61. See SASOT BETES, *supra* note 36, at 588-91.

lance committee, or by the IGJ officers.<sup>62</sup> Any claim brought by persons other than shareholders must be filed within three months<sup>63</sup> of the relevant meeting. The courts in this regard have restrictive criteria to protect the shareholders' interest and the operation of the corporation without damaging the shareholders' rights.<sup>64</sup>

- **Pre-emptive Right:**<sup>65</sup> The owners of common shares, whether single or multiple vote shares, are entitled to a pre-emptive right to subscribe additional shares offerings of the same class *pro rata* the number of shares held. They are also entitled to accrue *pro rata* the shares they subscribe on each occasion. Please bear in mind that if the company has gone public, the limitation set forth in section 216 of the ACL that states that no multiple vote shares will be issued applies.

The corporation shall offer the stock to the shareholders by publishing notices during three days in the Official Gazette; when corporations included in section 299<sup>66</sup> of the ACL are involved, notices also must be published in one of the leading Argentine newspapers. Shareholders may exercise their pre-emptive right within thirty days following the date on which the last notice was published, provided that the by-laws do not stipulate a longer period. When corporations make public offerings of stock, the extraordinary shareholders' meeting may reduce this term to a ten-day minimum term, both for their shares as well as for debentures convertible into shares. Shareholders shall also have a pre-emptive right to subscribe debentures convertible into shares.

- **Right to File Claims Against Directors:**<sup>67</sup> Both the company and the shareholders individually may file claims against directors of the corporation for breach of duties, violation of the law, violation of the by-laws or other internal regulations, damages caused by willful misconduct, or for abuse while in office or gross negligence. When we refer to the company, it has to be previously resolved by a shareholders' resolution.
- **Right to Obtain Copies of the Minutes of the Shareholders' Meetings:**<sup>68</sup> Any shareholder may request the board of directors, at his own expense, a signed copy of the meeting minutes. The board has the obligation to provide the requested copies.
- **Right to Request Judicial Overseeing of the Company:**<sup>69</sup> The share-

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62. ZUNINO, *supra* note 39, at 238.

63. Law No. 19.550, art. 251.

64. See CNCom. Room A, 87 E.D. 505 (1980); Rep L.L., XL-2432, summary 73; CNCom. Room B, [1982-A] L.L. 82; [1981-IV] J.A. 12; 91 E.D. 492; "Vistalba S.A. y otros c/Banco de Galicia y Buenos Aires S.A.," CNCom. Room A, [1987-D] L.L. 346.

65. Law No. 19.550, arts. 194, 195.

66. See *supra* note 18.

67. Law No. 19.550, arts. 276, 279.

68. *Id.* art. 249.

69. *Id.* arts. 113-117.

holders may request judicial overseeing (*intervención judicial*)<sup>70</sup> of the company as a preventive measure whenever the administrators of the company perform or omit actions that may result in serious danger to the company. To this extent, the following conditions are set forth: (i) his capacity as a shareholder; (ii) the existence of the danger and its seriousness; (iii) the fact that the shareholder has exhausted all remedies set forth in the by-laws; and (iv) the filing of an action for removal of the director.

- **Right to Dividends:**<sup>71</sup> The distribution of dividends or payment of interest to shareholders are legitimate only if they arise from earned and liquid profits corresponding to a balance sheet of a financial year correctly drawn up and approved. It is prohibited to distribute interests or dividends (i) in advance or provisionally or (ii) stemming from special balance sheets except in the companies covered by section 299<sup>72</sup> of the ACL. In all these cases the board of directors and the members of the statutory supervisor committee are jointly and without limit liable for such payments and distributions.

## 2. *Rights Pertaining to Certain Shareholders in Accordance with their Shareholdings*

Shareholders representing stated percentages of the capital stock are granted with additional rights as follows:

<i>Right</i>	<i>Description</i>	<i>Percentage of shareholding required to exercise the right</i>	<i>Section of the ACL</i>
<i>Right to request surveillance by the IGJ.</i>	The IGJ may, upon request, exercise supervisory functions in the case of public companies not included in article 299 <sup>73</sup> of the ACL.	10%	301
<i>Right to request partial distribution during the liquidation of the company.</i>	If a corporation is going through a liquidation procedure and liabilities were sufficiently guaranteed, then a partial distribution may be made upon the request of a shareholder.	10%	107

70. Consistent with the appointment of an inspector or a co-manager.

71. Law No. 19.550, art. 224.

72. See *supra* note 18.

73. In this case it shall be limited to events in which the request is grounded.



<i>Right</i>	<i>Description</i>	<i>Percentage of shareholding required to exercise the right</i>	<i>Section of the ACL</i>
<i>Right to object to the statutory supervisor's dismissal without cause.</i>	The by-laws shall specify a term during which the statutory supervisors are elected to hold office that cannot exceed three financial years. Nevertheless, they will remain in office until they are replaced. Their appointment may be revoked only by the shareholders' meeting, which may order it without cause, always provided that there is no opposition filed by 5 percent of the corporate capital. Any clause contrary to these provisions is null and void.	5%	287
<i>Right to object waiver of directors' or managers' liability.</i>	The liability of directors and managers vis-à-vis the company is extinguished by approval of their actions or by express waiver or by compromise resolved upon by the shareholders' meeting, provided such liability is not due to breaches of the law, by-laws or regulations, and provided there are no objections from at least 5 percent of the corporate capital.	5 %	275
<i>Right to request the summons of a meeting.</i>	Ordinary and extraordinary shareholders' meetings shall be called by the board of directors or the statutory supervisor in those cases provided by law or whenever either may deem it necessary or when so required by shareholders representing at least 5 percent of the capital stock, provided the by-laws do not fix a lesser percentage. In the latter case, the petition will include the agenda to be dealt with, and the board of directors or the statutory supervisor shall summon the meeting to be held within the maximum term of forty days after the petition has been received. Should the board of directors or statutory supervisor fail to do so, the meeting may be called by the IGJ or by court order. <sup>74</sup>	5%	236

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74. MASCHERONI, *supra* note 33, at 31-32.

<i>Right</i>	<i>Description</i>	<i>Percentage of shareholding required to exercise the right</i>	<i>Section of the ACL</i>
<b><i>Right to obtain information from the statutory supervisor.</i></b>	The statutory supervisor, without detriment to other powers and duties provided by the ACL and conferred upon him by the by-laws, shall furnish shareholders, at any time required by the latter, with information on the subjects within his competence.	2%	294, sub-section 6
<b><i>Right to report irregularities.</i></b>	The statutory supervisor, without detriment to other powers and duties provided by the ACL and conferred upon him by the by-laws, shall investigate written complaints filed by shareholders and mention them in an oral report to the shareholders' meeting with pertinent considerations and proposals. He shall immediately call a shareholders' meeting to decide on the matter when the board of directors does not properly deal with the situation under investigation and he deems it necessary to proceed urgently.	2%	294, sub-section 11

#### IV. THE BOARD OF DIRECTORS: THEIR MEETINGS AND DUTIES

##### A. FUNCTION OF THE BOARD OF DIRECTORS

The company's administration will be in charge of a director or a board of directors appointed by the shareholders meeting or by the vigilance committee in accordance to the by-laws. The by-laws will set the number of directors to be appointed. In most cases, the by-laws set a range of directors that can be appointed (a minimum and maximum number), and then the shareholders decide the exact number to be appointed. If the company falls under the provisions set forth under section 299 of the ACL,<sup>75</sup> the board of directors must have at least three members.<sup>76</sup> In the event that the by-laws enable the shareholders to determine the number of members of the board of directors, the by-laws will specify the minimum and maximum allowed number of directors. Also, the by-laws should specify the term of duration of the office of the members of the board. Notwithstanding, it should be borne in mind that the term could not exceed three fiscal years and that the directors will remain in office until the new board has been appointed.<sup>77</sup>

Directors may be re-elected and once they have been appointed, they

75. See *supra* note 18.

76. Law No. 19.550, art. 255.

77. The fact that they should remain in office until a new board appointment is resolved implies that in some cases directors can exceed the three-year term established by section 257 of the ACL. *Id.* art. 257.

can only be removed exclusively by the shareholders' meeting.<sup>78</sup> Directors do not need to be shareholders. An absolute majority of directors must have their domicile of choice within the Republic of Argentina.<sup>79</sup> All directors shall establish a special domicile within Argentina where all notices concerning the performance of their duties, including those relative to action for liability, shall be valid.

The by-laws may provide for the election of alternate directors to substitute the lack of regular directors for any reason. This provision is compulsory for companies that dispense with the appointment of statutory supervisors.

The board of directors must accept and record in the pertinent minutes the resignation of any director at the first meeting held after it is tendered, provided this does not affect its regular work and is not fraudulent or untimely. Otherwise, the resigning director must continue in his capacity until the next shareholders' meeting decides the matter.

The by-laws must regulate the organization and working of the board of directors. Quorum may not be less than an absolute majority of its members. Decisions must be made by a majority, understood as the absolute majority of those present, although (as we mentioned in regard to the shareholders' resolutions regime) the by-laws can establish a more rigorous voting regime. Those directors who have an interest contrary to that of the company may not participate in a meeting of the board. The board of directors shall meet at least once every three months unless the by-laws require a greater number of meetings, without detriment to those that may be held at the request of any director.

The position of director is personal and cannot be delegated. Directors remain ultimately responsible. Directors cannot vote by mail, but can empower other directors to vote on their behalf, provided that there is quorum and their liability will be the same as that of directors present at the meeting.<sup>80</sup>

The board of directors of an issuing entity may conduct meetings in the physical presence of its members or via a communications system that provides for a simultaneous transmission of sound, images or words, when the by-laws establishes so. The statutory supervisor committee shall indicate the regularity of the adopted decisions. As we previously mentioned in regard to the representation through a proxy granted in favor of another member of the board, only present members shall be computed as quorum unless the by-laws otherwise establishes. The by-laws may establish that the meetings may be held at a distance.<sup>81</sup> The application of these procedures recently incorporated by the TD, should

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78. *Id.* art. 256.

79. In order to avoid any misinterpretation, it should be borne in mind that this requirement only applies to the regular directors and not to the alternate directors that will not be considered as appointed directors, unless they perform any duty on behalf of their office.

80. Law No. 19.550, art. 266.

81. Law No. 17.811, art. 65.

also be extended to the shareholders' meetings because the only way to celebrate them is by the physical presence of the shareholders or by the physical presence of someone holding a proxy. As a matter of accuracy, the meeting procedures should ensure that votes are properly counted and recorded, and that a timely announcement of the outcome be made.<sup>82</sup>

According to labor and social security regulations, the relationship between the directors and the company is similar to that of an employment contract without the element of dependence. Therefore, the director is a corporate official who is a part of the administrative body of the company.<sup>83</sup>

Among the rules of the so-called "Public Offering Transparency Regime," section 8 of the TD establishes that when exercising their functions, directors and managers shall act in a loyal and diligent manner, bearing in mind the following guidelines in particular:

- (i) To place the corporate interests of the issuer where they perform duties and the common interest of the shareholders above any other interest, including the controlling shareholder's interests;
- (ii) To refrain from obtaining a personal benefit from the issuer other than the compensation paid for their functions;
- (iii) To organize and implement preventive systems and mechanisms to protect the corporate interests, thus reducing the risk of conflicts of interests, either permanent or temporary, in the personal relationship with the issuer or with persons related to the issuer;<sup>84</sup>
- (iv) To make the necessary arrangements to perform the issuer's activities and implement the necessary internal control to ensure a careful management and avoid breaches of the duties established by the regulations of the CNV and of self-regulated entities; and
- (v) To act with due diligence when preparing and disclosing the information to the market, and maintain the independence of external auditors.

## B. MANAGERS

The board of directors can designate general or special managers, who may or not be directors. Directors will be able to delegate administrative executive matters. At any time, these "special designations" may be revoked. They are responsible to the company and third parties for the performance of their assigned duties to the same extent as the directors.<sup>85</sup>

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82. *OECD*, *supra* note 3, at 29.

83. *VERÓN*, *supra* note 36, at 16.

84. This duty specifically refers to activities competing with the issuer, the use or imposition of a lien on corporate assets, the determination of compensations or proposals related thereto, the use of non-public information, the use of business opportunities for their own benefit or for the benefit of third parties, and in general, any situation that may generate a conflict of interests affecting the issuer.

85. Law No. 19.550, art. 270.

The appointment of general or special managers does not exclude directors' liabilities related to their mandatory duties.

The position of the managers should not be confused with that of the directors. The differences result from the manner of their designation, removal, and liability. Managers are designated and removed by the board of directors while directors are appointed and removed by the shareholders' meeting. Further, the liability of the managers arises by the guidelines set forth by the board of directors whose guidelines are established by the shareholders in accordance to the by-laws of the company. In sum, unlike directors who are officers of the company, managers are employees.

### C. DIRECTORS AND MANAGERS LIABILITY: LOYALTY AND DILIGENCE

The directors, managers, and representatives of the company must act with loyalty and with the diligence of a good businessman.<sup>86</sup> The duty to act loyally embraces a prohibition against any director competing with the corporation. Encompassed within the standard that directors act with the diligence of a good businessman are the requirements that directors possess certain qualifications (e.g., technical knowledge, expertise, etc.) and that directors perform their responsibilities in accordance with such qualifications.<sup>87</sup>

According to the principles of loyalty and diligence of a good businessman, directors are unlimitedly and jointly and severally liable vis-à-vis the company, the shareholders, and third parties for the improper performance of their office. Directors are likewise liable for breaches of the law, by-laws or regulations, and for any damage caused by fraud, abuse of powers or grave negligence.<sup>88</sup>

This charge of liability shall take into account individual performance when duties have been assigned personally according to the provisions of the by-laws, regulations or resolutions adopted by the general shareholders' meeting. A director who took part in the discussion or resolution or was aware of it, shall be exempted from liability if he puts his protest on record in writing and gives notice thereof to the statutory supervisor before his liability is reported to the board of directors, the statutory supervisor, the shareholders' meeting, the IGJ or before an action is brought before the courts.

Directors and managers may be freed from liability for certain decisions upon subsequent approval by the shareholders at a shareholders' meeting, provided that such decision did not violate the law or the by-laws and there is no objection by any shareholder representing 5 percent

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86. *Id.* art. 59.

87. MARIANO GAGLIARDO, *RESPONSABILIDAD DE LOS DIRECTORES DE S.A.* 570 (1994).

88. In addition to the potential civil liability faced by directors, in accordance with sections 173 subsection 7, 300 subsection 3, and 301 of the Argentine Criminal Code, directors who fraudulently breach their obligations may be imprisoned.

or more of the company's capital.<sup>89</sup> Directors will not be held liable for negative downturns in the corporation's business (e.g., losses) if such consequences are not a result of the directors' breach of their duties.

Although the law establishes that the liability of managers has the same breadth as that of directors, as mentioned in the previous section, it is important to emphasize that the liability of the managers is not several.<sup>90</sup> They are governed by the general rules of agency and tort of the Argentine Civil Code, as well as by the Employment Contract Law, which holds employees liable to their employers for damages caused by fraud or gross negligence.

## V. SPECIAL REQUIREMENTS AND APPLICABLE PRACTICES FOR PUBLIC OFFERING COMPANIES

### A. AUDITING COMMITTEE: MEMBERS AND FUNCTIONS

As we previously mentioned in section II of this article companies making public offering of their shares of stock shall create an audit committee. The audit committee shall consist of three or more members of the board of directors, the majority of which shall be independent pursuant to the criteria established by the CNV. The auditing committee shall have the following powers and functions:

- (i) Give an opinion to the proposal of the board of directors for the appointment of external auditors to be hired by the company, and control their independence.
- (ii) Supervise the performance of the internal control systems and of the administrative-accounting system. Supervise the trustworthiness of the administrative-accounting system, the financial information and other relevant events submitted to the CNV, and to self-regulated entities pursuant to the applicable information regulations.
- (iii) Supervise the application of the information policies with regard to the company's risk management.
- (iv) Provide the market complete information with regard to transactions where there is conflict of interests with members of corporate bodies or controlling shareholders.
- (v) Give its opinion about the reasonability of the proposals on fees and option plans for directors or managers of the company made by the management body.
- (vi) Give its opinion about the performance of the legal requirements and the reasonability of the conditions to issue shares or securities convertible into shares, in the case of capital increase excluding or limiting the pre-emptive right.
- (vii) Verify the performance of the applicable behavior rules.

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89. Law No. 19.550, art. 275.

90. RICARDO AUGUSTO NISSEN, *LEY DE SOCIEDADES COMERCIALES: COMENTADA, ANOTADA Y CONCORDADA* 356 (1996).

- (viii) Give a well-founded opinion with regard to operations with related parties.
- (ix) Give a well-founded opinion and communicate it to self-regulated entities pursuant to what is determined by the CNV whenever there is, or there may arise, a conflict of interest in the company.

Once a year, the audit committee shall prepare a plan for the fiscal year that will be submitted to the board of directors and to the statutory supervisor committee. The audit committee shall have access to the information and documents it may deem convenient for the performance of its obligations.

## B. DISCLOSURE AND TRANSPARENCY

### *1. Disclosure Obligations Imposed on Certain Participants in the Market*

“A strong disclosure regime is a pivotal feature of market-based monitoring of companies and is central to shareholders’ ability to exercise their voting rights” and it can also “help to attract capital and maintain confidence in the capital markets.”<sup>91</sup> The ACL, TD, CNV, and IGJ’s rules settle the major framework of the duty to disclose.

The by-laws of companies as well as its amendments, and the board appointments are publicly available through the IGJ. Corporations have the mandatory duty to file with the IGJ any amendment to its by-laws<sup>92</sup> and any amendment in the composition of the board of directors.<sup>93</sup> Once a year, non-public offering companies also have to submit their financial statements with the IGJ.<sup>94</sup> Also, it is mandatory to public offering companies to submit copies of quarterly financial statements and annual reports, together with information about members of the board and the statutory supervisory committee to the CNV and the relevant stock exchange. Pursuant to section 5 of the TD, certain officers and parties of the companies offering securities have certain disclosure requirements to the CNV, the stock exchange, and the public domain. This disclosure is focused in the occurrence of “material events” (*hechos relevantes*) that might affect the price of the securities or the negotiation itself. Although the scope of “material events” is not established, the TD provides the following events and circumstances as disclosure events:

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91. *OECD*, *supra* note 3, at 29.

92. Law No. 19.550, art. 10.

93. *Id.* art. 60.

94. *Id.* art. 67.

<i>Disclosure to the CNV</i>	
<i>Parties</i>	<i>Issues to disclosure</i>
Directors and managers of issuers making public offering of negotiable securities and the members of the statutory supervisor committee.	Any event or situation that, due to their importance, may substantially affect the underwriting of the negotiable securities or their negotiation.
Intermediaries authorized to act in public offerings.	Any unusual event or situation that, due to its importance, may affect the business, responsibility or decisions with regard to investments.
Directors, auditors, managers, and the members of the statutory supervisor committee (both permanent and alternate members), as well as the controlling shareholders of issuers making a public offering of their negotiable securities.	The number and class of shares of stock and debt bonds convertible into shares, and options of negotiable securities held by them in any related entity.
Members of the qualification council, directors, managers, auditors or members of the statutory supervision committee (either permanent or alternate members) of risk rating agencies.	The number and classes of shares of stock, debt bonds or options held by them.
Directors and officers of the CNV, self-regulated entities, and securities depositories.	The number and classes of shares of stock, debt bonds, and options held by them in companies authorized to make public offerings of their negotiable securities.
Any person or legal entity that, either directly or through other persons or legal entities, or all the persons belonging to groups acting in a coordinated way, purchases or sells shares of stock in a company making public offering of its negotiable securities for an amount that implies changes in the stakes held by the controlling group or groups, and thus affecting the structure.	Any transaction or group of transactions made in a coordinated way.
Any person or entity that is not comprised by the above paragraph and that, either directly or through other persons or legal entities, or all the persons forming groups that act in a coordinated way, purchases or sells shares of stock of an issuer whose capital stock is comprised by the public offering system and that grants 5% or more of the votes for the purposes of making corporate decisions at general shareholders' meetings.	The transactions that grants 5% or more of the votes for the purposes of making corporate decisions at general shareholders' meetings.



<i>Disclosure to the CNV</i>	
<i>Parties</i>	<i>Issues to disclosure</i>
Any entity or individual entering into shareholders' agreements or understandings aimed at exercising the voting right in a company whose shares are publicly offered or in the company controlling it, including but not limited to: agreements creating the obligation to consult prior to exercising the vote that limit the transfer of the corresponding shares or negotiable securities; granting the right to purchase or subscribe them, or establishing the purchase of said securities; and, in general, having as object or effect the joint exercise of a dominant influence in said companies or substantial changes in the structure or power relationships in the corporate governance.	Said agreements, understandings or changes.

The Rules of the CNV provide that the directors and statutory supervisors may request the CNV to suspend their duty to disclose to the market certain information, which may seriously affect the corporate interest. The CNV in this case can issue a grounded decision suspending such duty for a limited time.

The public shall be informed of the name of the negotiable security, the amount, price, and moment when the transactions are completed on an authorized market. Also, it must be informed of any intermediaries of the corresponding market that have participated in the transactions and the type of their participation. Moreover, information on stock options, benefit plans, and remuneration paid to directors and top executives must be informed in the prospectus when registered securities are issued. Finally, persons who, in the course of a public offering, with fraud or gross fault, disclose false news without regard to the benefits for themselves or for third parties or damages to third parties, including the issuer, shall be subject to the penalties.<sup>95</sup> This practice known as "market price manipulation" intends to (i) artificially affect the price or liquidity of the negotiated volume of one or more securities or (ii) mislead any market participant. Misleading action comprises false statement uttered knowing its inexact or misleading nature, as well as omissions to provide essential information when such omission may induce mistakes to third parties.

The Argentine Criminal Code states that any person who (i) maneuvers to raise or lower the price of stocks or public funds by means of false news, fake negotiations or by means of an understanding among the principal holders of goods or securities, in order not to sell or to sell at a certain price; or (ii) publicly offers funds or securities simulating or hiding facts or true circumstances or affirming or showing in any manner the occurrence of false facts, shall be imprisoned for six months to two

95. These penalties are established in section 10 of the SL and its amendments, and vary from warnings, fines up to temporal or definitive prohibitions. Law No. 17.811, *supra* note 26, art. 10.

years.<sup>96</sup> Civil actions claiming torts could also apply based on the damage produced.

## 2. *Insider Trading*

The basic premise of insider trading is that any person who has access to confidential or privileged information<sup>97</sup> due to his position, must refrain from trading any securities related with such information, and must maintain reserve with respect to any information which may affect their sale until such information is disclosed to the market. The TD<sup>98</sup> imposes a reserve duty to these persons.

Directors, managers, auditors, members of the statutory supervisory committee, controlling shareholders, and professionals participating in an entity authorized to make public offering of negotiable securities, or a person making a bid to purchase or swap securities of an entity authorized to make public offering, and agents and intermediaries in the public offering, including financial trustees, managers, and depositories of investment funds; and in general, any person who by virtue of his position or activity has information with regard to an event that has not been publicly disclosed, and that due to its importance may affect the underwriting or negotiations of the negotiable securities in an authorized public offering or forward contracts and options, shall be strictly confidential and shall refrain from negotiating until said information is publicly disclosed.<sup>99</sup> The Commercial Court of Appeals has considered<sup>100</sup> that inside information do not need to be such that actually affects the placement of securities or their market price, but also such that may affect its placement or price. Furthermore, public officers, authority officers, and employees of risk rating agencies, and of public or private controlling entities including the CNV, self-regulated entities and securities depositories, and any other person who, by virtue of his functions, has access to similar information, shall hold it in confidence.

The duty of confidentiality is extended to those persons that due to a temporary or accidental relationship with the company or with the above mentioned persons may have access to the described information and, additionally, to employees and third parties that due to the nature of their functions may have had access to the information.

On July 11, 1996, through resolution 11,377 the CNV imposed a fine to certain managers and directors of *Establecimiento Modelo Terrabusi S.A.*

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96. Cód. Pen. § 300.

97. Including any concrete information related to one or several securities or to one or several issuers that has not been disclosed, and that if disclosed may substantially affect or have affected the underwriting conditions or price or the negotiation of said securities.

98. Decree No. 677/2001, art. 7.

99. This reflects the "abstain or disclose" rule issued by the SEC in relationship with *In re Cady, Roberts & Co.*, 40 S.E.C. 907 (1961); *SEC v. Tex. Gulf Sulphur Co.*, 401 F.2d 833 (1968); *Shapiro v. Merrill Lynch*, 495 F.2d 228 (2d Cir. 1974).

100. "Establecimiento Modelo Terrabusi s/transferencia de paquete accionario," CNCom. 117 E.D. 29 (1997).

(the Defendants). This fine was imposed due to the breach of CNV's general resolution 227/93,<sup>101</sup> by the performance of insider trading practices. Because the major aim of the Court of Appeals (Room A)<sup>102</sup> was to preserve the market's transparency, it resolved the case in the same line of thinking of the CNV by confirming and ratifying the fine imposed to the Defendants. The Defendants appealed the resolution of the Court of Appeals<sup>103</sup> before the Supreme Court.<sup>104</sup> After analyzing the case, the Supreme Court revoked the Court of Appeals' decision, arguing that it was not sufficiently grounded and that some of the conclusions were based only on assumptions<sup>105</sup> that obliged the Court of Appeals to issue a new judgment.

Although it commented on insider trading, the Supreme Court's ruling was focused on the procedural aspects. Unfortunately, these comments were enough to condition the Court of Appeals' (Room D) new resolution<sup>106</sup> that finally revoked the CNV's resolution 11,377 and the applicable fines. This was the first case dealing with "insider trading," and it was a great opportunity to establish a very important precedent. The only remaining comfort after the analysis of the procedural stages is that at least the CNV, the Court of Appeals (Room A), and the Supreme Court's dissenting opinion agreed, although they did not impose their way of thinking with which we agree. Sooner or later there will be a wind of change,<sup>107</sup> and the line of thinking of this judgment will be reverted.

The OECD Principles of Corporate Governance comments that:

The Principles of Corporate Governance reaffirm that it is reasonable for investors to expect that the abuse of insider power be prohibited. In cases where such abuses are not specifically forbidden by legislation or where enforcement is not effective, it will be important for governments to take measures to remove any such gaps.<sup>108</sup>

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101. This resolution was (i) formerly CNV's general resolution 190, and (ii) restated by TD.

102. Acting as the appellant body of an administrative first instance.

103. It is important to point out that in this case, one of the main defensive lines was very similar to the facts discussed in *SEC v. Falbo*, 14 F. Supp. 2d. 508 (S.D.N.Y. 1998).

104. "Establecimiento Modelo Terrabusi s/transferencia de paquete accionario," CSJN 5 E.D. 3 (2002).

105. Note that the dissenting opinion argued that the family relationship is not a minor issue and that it should be taken into account to demonstrate the insider trading practices based on the U.S. cases: *SEC v. Tex. Gulf Sulphur Co.*, 401 F.2d 833 (1968) and *U.S. v. Chestman*, 947 F.2d 551 (2d Cir. 1991).

106. *Comisión Nacional de Valores c/ Establecimiento Modelo Terrabusi SA s/ Transferencia paquete accionario a Nabisco*, Resolution N. 11.377 CNCom. Room D, LL, Feb. 19, 2003, 6 (1996).

107. There are many legal authors that think the same way. For example, Rodrigo S. Luchinsky comments on the Supreme Court's resolution on Aug. 27, 2002. See *Errepar* – D.S.E. N° 175, June 2002, Vol. XIV, at 265.

108. *OECD*, *supra* note 3, at 34.

### 3. *External Auditors*

Financial statements of companies making public offerings of their securities shall only be audited by accountants who have previously submitted an affidavit informing the CNV of any criminal, administrative or professional penalties previously imposed on them, except the professional ones that have been assessed as private by the competent professional council. Such information shall be permanently updated by the interested parties and shall be disclosed to the public through the procedures established by the regulations of the CNV.

The shareholders' general meeting, when approving the financial statements, shall appoint independent chartered accountants to be in charge of the external audit corresponding to the new fiscal year. At any time, the shareholders' meeting may revoke the appointment when there are enough reasons. If the administration body makes the appointment proposal, the audit committee shall analyze it just as if the same body recommends the revocation of their duties.

## C. CORPORATE CONTROL

### 1. *Anti-Takeover Devices*

Neither the ACL nor the TD or other rules expressly address anti-takeover devices. Common practice defensive measures, however, include: (i) provisions within the by-laws restricting share transfers;<sup>109</sup> (ii) shareholders' agreements; (iii) increased quorum and supermajority requirements for shareholder meetings; (iv) issuance of participation bonds or non-voting shares; (v) golden parachutes; (vi) poison pills; (vii) staggered term boards; and (viii) scorched-earth defense.<sup>110</sup> We will not refer in detail to these practices because they are very well known and they are not the core subjects of this paper.

### 2. *Public Offering*

In addition, the TD establishes that a public offering of voting shares of a company, whose shares are available on a public offering system, shall be addressed to all holders of said shares. In the case of binding offerings, the public offering of voting shares shall further include the holders of (1) subscription rights or stock options, and (2) convertible debt securities or other similar securities that in a direct or indirect way may grant a

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109. Share-transfer restrictions are allowed provided that they are expressly contemplated in the by-laws (which imply that is known by all the parties related to the company) and that they do not entail outright prohibitions to transfer such shares. The implementation of such restrictions is generally vested on the board.

110. According to the AAI Journal, published in Chicago in 1986 by the American Association of Individual Investors, this is a tactic in which the defending company's management engages in practices that reduce their company's value to such a degree that it is no longer attractive to the potential acquirer. It is important to point out that this practice, as well as any other intent by the board to stop a takeover bid, would be in the interest of the company. Otherwise, they could be acting only for their own purposes.

subscription, acquisition or conversion right on voting shares proportionate to their holdings and in the amount of the holding to be acquired.<sup>111</sup>

### 3. *Binding Public Offering and Significant Stake*

The person or entity who, with the intention to obtain direct or indirect control of a company whose shares are admitted by the public offering system, proceeds to acquire – acting individually or in agreement with other persons, in a unique act or successive acts – for valuable consideration a number of voting shares of subscription rights, stock options, convertible debt securities or other similar securities directly or indirectly granting a subscription, acquisition or conversion right on voting shares or a “significant stake” (e.g., 35 percent) in the corporate capital shall previously carry out a binding public offer or securities swap. The binding system, however, shall not apply to the acquisition of shares or other securities as long as, as a whole they do not exceed such “significant stake.” Neither shall apply in the cases where a change of control takes place as a consequence of the company’s restructure, merger or spin-off.

The TD also introduced a system of residual stakes,<sup>112</sup> which apply to all listed companies. This system establishes that when a shareholder, either directly or through one or more controlled companies holds 95 percent or more of the subscribed capital (the so called “almost total control”), he is obliged upon the request of any minority shareholder to make an offer to purchase all of its shares. In addition, within a six-month term from the date when a person obtained the company’s “almost total control,” the person may issue a unilateral statement of its decision to acquire the total remaining corporate shares held by third parties.

## VI. CONCLUSION

The set of rules required to have a complete corporate governance framework has already been enacted. All the relevant OECD Principles of Corporate Governance are included in the Argentine legal framework. Only some operational rules of minor importance have not been incorporated. Although the rules are sufficient, the belief that enactment of new rules can improve markets remains to be a problem of considerable importance. To the contrary, however, new rules only provide a continuous basis of change, thus frightening investors.

The OECD Principles of Corporate Governance further provide that:

Of particular relevance is the relation between corporate governance practices and the increasingly international character of investment. . . . If the countries are to reap the full benefits of the global

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111. The major aim of these provision set forth by the TD is the equal treatment among shareholders, both as to economic and financial conditions and as to any other acquisition condition for all shares, securities or rights of the same category or class.

112. Decree 677/2001, §§ 25-28.

capital market, and if they are to attract long-term “patient” capital, corporate governance arrangements must be credible and well understood across borders.<sup>113</sup>

Yet, significant structural issues remain unresolved. Backlogs and poor judicial systems, as well as the implementation, effectiveness, and enforcement of the new laws and regulations remain untested.<sup>114</sup>

Unfortunately, standards or rules alone are insufficient if they are not supported by the right culture, ethics, and professionalism.<sup>115</sup> On the international field, Enron and WorldCom were horrible corporate governance failures.<sup>116</sup> This proves that no country is exempt. Although Argentina is in the right path with its intent to enter into the globalized market,<sup>117</sup> many things still have to be done, including a departure from a vigorous enforcement of the law. Argentina requires a well-functioning judicial system to provide efficient remedies and rational outcomes. The piercing of the corporate veil by the Labor Court of Appeals in the *Delgadillo Linares, Adela c/Shatell SA y otros s/Despido* and *Duquelsy, Silvia c/ Fuar SA y otro* cases as well as the lack of punishment to the insider traders in the *Establecimiento Modelo Terrabusi s/transferencia de paquete accionario* case are clear examples of legal risks that undermine legal certainty.

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113. OECD, *supra* note 3, at 12.

114. *Global Investing: Be Nice to Minorities in Latin America*, FIN. TIMES, July 23, 2001, at 20. Moreover, *The Economist* anticipated what would happen in Argentina in the event that stricter standards were adopted: “Draft guidelines drawn up by the OECD and Brazil, Chile and Argentina propose strict new standards for multinational firms in areas such as the environment and corporate governance. Even if approved, they will be hard to enforce in emerging economies.” *Business This Week*, THE ECONOMIST, Jan. 15, 2000, at 7.

115. BERGHE & RIDDER, *supra* note 5, at 20.

116. William S. Lerach, *Plundering America: How American Investors got Taken for Trillions by Corporate Insiders – The Rise of the New Corporate Kleptocracy*, 8 STAN. J.L. BUS. & FIN. 69 (2002).

117. For example, Argentina had celebrated an inter-agency memoranda of understanding with the U.S. Securities Exchange Commission for the provision of reciprocal assistance in obtaining documentary and testimonial evidence. In 1988, the U.S. Congress passed the International Securities Enforcement Cooperation Act, which allows the Commission to assist foreign securities authorities with their investigations even when no violations of U.S. laws are at stake. David. M. Stuart & Charles F. Wright, *The Sarbanes-Oxley Act: Advancing the SEC’s Ability to Obtain Foreign Audit Documentation in Accounting Fraud Investigations*, 2002 COLUM. BUS. L. REV. 749 (2002).

