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The United States securities experience includes, in addition to the Federal Securities Act of 1933, a second stage of regulation, the Securities Exchange Act of 1934.[145] The principal focus of the 1934 Act was the regulation of trading in securities after their initial issuance. The government's general intent here was to regulate the securities markets and the activities of broker-dealers.[146] To some degree the Venezuelan Capital Markets Law also attempts to do this.

Under the 1934 Act there are two key informational requirements. Section 12 of the 1934 Act[147] requires registration of any security that is traded on a national securities exchange, or an equity security where the corporation has total assets in excess of $1 million and the security is held by 500 or more persons.[148] Also, a corporation with a security registered under Section 12 must file periodic reports with the SEC so as to keep current the information contained in the original filing.[149]

The Venezuelan law is similar to the 1934 Act up to this point. The Venezuelan law does not expressly provide for registration of any security on the basis of its being traded on a national securities exchange or being issued by a company with a certain bolivar amount of assets. Rather, Article 17 of the Venezuelan law[150] generally provides that all securities which are publicly offered under the terms of the Capital Markets Law are subject to the control of the CNV.[151] In this regard, the Venezuelan law has apparently combined into

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[145]15 U.S.C. § 78a *et seq.*, (1970).
[146]W. CARY, CORPORATIONS, 297-98 (1969).
[147]15 U.S.C. § 781 (1970).
[148]*Id.*
[149]*Id.*
[150]1973 Law, art. 17, at 3.
[151]*Id.*

one overall registration requirement the registration information which is required to be filed separately under the Federal Securities Act of 1933 and the Securities Exchange Act of 1934.

The Venezuelan law also provides for the filing of periodic reports with the CNV so as to update the original registration information.[152] All companies whose securities are listed in the National Securities Register[153,154] are subject to this periodic filing requirement.[155] Information which must be provided annually includes a balance sheet, profit and loss statement, and statements as to movement of surplus and working capital accounts, all to be certified by an independent public accountant.[156] A report dealing with the financial condition of the company is also to be filed twice a year.[157] The latter section is especially vague and ambiguous, since there is no indication as to what type of financial information is required. Additionally, a special report must be made to the CNV when a company which has previously made a public offering has entertained proposals for a merger, an increase or decrease in capital, a change in corporate purpose, or entering into a substantial transfer of assets.[158] Once again the author notes that this provision is especially vague in that it does not provide any time limits as to filing or indication of what constitutes a "substantial transfer of assets" or what is considered to be a "change in corporate purpose."

The financial reporting requirements of the Venezuelan law take on added importance in view of the broad grant of authority given to the CNV to effectuate the law. In regard to the annual reporting requirements, the CNV is specifically authorized to require submission of any information which it deems necessary to enforce the law.[159] In the section dealing with the special filing report[160] for mergers and change of corporate purpose, the CNV is empowered to require submission of whatever information it deems necessary. The broadest grant of inspection authority given to the CNV is found in Article 116.[161] Specifically, the CNV is able to carry out inspection of the books of *any* company if it believes it necessary to properly analyze the financial statements submitted by another company.[162] This right of inspection by the CNV is not unlimited, however, since the confidentiality requirements of Arti-

[152]*Id.* art. 112, at 12.
[153]*Id.* art. 10, § 7, at 2.
[154]*Id.* art. 14, at 3.
[155]*Id.*
[156]*Id.* art. 112, § 1,5, at 12.
[157]*Id.* § 2, at 12.
[158]*Id.* art. 115, at 12.
[159]*Id.* art. 112, § 7, at 12.
[160]*Id.* art. 115, at 12.
[161]*Id.* art. 116, at 12.
[162]*Id.*

cle 16 apply.[163] As such, this specially obtained information will not necessarily be made public, since Article 16 gives the CNV the authority to designate any information obtained by it as confidential.[164]

The Venezuelan Capital Markets Law left untouched a number of areas which are of paramount importance under the 1934 Act. Two of the most important enforcement provisions of the 1934 Act are Section 10(b)[165] and SEC Rule 10b-5.[166] Section 10(b) makes it unlawful to "use or employ . . . any manipulative or deceptive device in contravention of such rules . . . as the [Securities and Exchange] Commission may prescribe" in connection with the purchase or sale of any security.[167] The SEC promulgated Rule 10b-5 in order to implement Section 10(b). Rule 10b-5 makes it unlawful to do any of the following things in connection with the purchase or sale of any security: 1) to employ any device, scheme, or artifice to defraud; 2) to make any untrue statement of a material fact or to omit a material fact necessary in order to make the statements not misleading; or 3) to engage in any act, practice or course of business which operates as a fraud or deceit upon any person.[168] Section 10(b) does not expressly provide for a civil remedy. However, Section 10(b) and Rule 10b-5 together implicitly create a right of action in favor of the injured party.[169,170]

There are a number of key elements for an action to be brought under Section 10(b) and Rule 10b-5. First, there must be manipulative or deceptive conduct on the part of the defendant. Second, where the alleged violation concerns misrepresentation or nondisclosure, it must be shown that the information at issue was material. Third, in any private action for damages liability cannot be based on negligent conduct alone; rather, there must be a showing of the defendant's intent or scienter.[171] Reliance or causation was previously believed to be an essential element of a 10b-5 action (i.e., it must appear that the plaintiff in some way relied on the defendant's misrepresentation or nondisclosure).[172] However, the importance of this element has been lessened by recent Supreme Court holdings.[173]

Under the 1934 Act the following hypothetical situation would be regulated:

[163] *Id.* art. 16, at 3.
[164] *Id.*
[165] 15 U.S.C. § 78j (1970).
[166] 17 C.F.R. § 240.10(b)-5 (1976).
[167] 15 U.S.C. § 78j (1970).
[168] 17 C.F.R. § 240.10(b)-5 (1976).
[169] Sup't of Insurance v. Bankers Life & Casualty Co., 404 U.S. 6 (1971).
[170] Kardon v. National Gypsum, 203 F.2d 627 (2d Cir. 1973).
[171] Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976).
[172] List v. Fashion Park, 340 F.2d 457 (2d Cir. 1975).
[173] Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972); Mills v. Electric Auto-Lite, 396 U.S. 375 (1970).

the management of the fictional CATC [introduced earlier as the company in which Señor Diaz has a minority shareholder interest] issued a press release to the *Venezuelan Commercial Journal* on January 1, 1977. This press release was designed to quell rumors which had been circulating for over one month about a rich iron ore strike by a subsidiary of CATC in the interior of Venezuela. The statement indicated that recent reports exaggerated the scale of operations and mentioned plans and statistics of size and grade of ore that were without factual basis and were evidently originated by speculation of people not connected with CATC. The statement to the *Journal* indicated that CATC's subsidiary had been conducting some mineral exploration in the interior for six years and that this was simply one part of the overall search for various minerals. Some core drillings in the Zapara mineral tract had recently been undertaken as part of the program. The statement further noted, however, that the work done to date had not been sufficient to reach definite conclusions, and any report as to size and the grade of ore would be premature and probably misleading. In fact, as of January 1, 1977, the management of CATC knew that drilling tests had been successfully completed and that a major iron ore discovery had been made by the company. Based upon this information Señor Diaz, on January 2, 1977, decided to sell 500 shares of his stock in CATC. Subsequently, it was learned that these shares were immediately purchased by the Sanchez brothers. On February 1, 1977 Señor Diaz learned that his prior decision was hasty, for on that day CATC announced a major iron ore discovery in the Zapara region. Thereafter, CATC's stock climbed to unprecedented heights.

The previously mentioned statements of the management of CATC apparently are not regulated by the Venezuelan Capital Markets Law. The administrative and penal provisions of the law do not address themselves to making unlawful any manipulative or deceptive device in connection with the purchase or sale of any security. Rather, the emphasis of the law's three main enforcement provisions is on ensuring compliance with registration information requirements; to this end the law makes it unlawful to submit false information to the CNV.[174] The absence in the Venezuelan Capital Markets Law of protective devices such as Section 10(b) and Rule 10b-5 is especially important, since the practical effect of these two provisions is to encourage enforcement of the 1934 Act by allowing a private cause of action. The SEC cannot investigate and discover every securities violation.[175]

Another important enforcement provision of the 1934 Act is Section 16,[176]

[174]1973 Law, arts. 146, 148, 149, at 14-15.
[175]Kardon v. National Gypsum, 203 F.2d 627 (2d Cir. 1973).
[176]15 U.S.C. § 78p (1970).

which deals with "short-swing" profits resulting from trading in the company's shares by certain types of insiders. Section 16(a) has a specific disclosure requirement whereby every person who, directly or indirectly, is the beneficial owner of more than 10 percent of any class of security which is registered under Section 12 of the Act,[177] or who is a director or officer of the corporation which has issued securities, must file periodic reports showing the amount of the company's securities which he beneficially owns, or any changes in his holdings. These reports must be filed with the SEC and with any national securities exchange on which the stock is traded. An initial report must be filed within ten days after a person has become a 10 percent shareholder, officer, or director. Under Section 16(b), any profit realized by an "insider" from the purchase and sale, or any sale and purchase of the company's securities within any period of less than six months is recoverable by the company.[178]

The Venezuelan Capital Markets Law does not expressly deal with the problem of "insider" trading. There is no disclosure requirement for the three "insider" groups—10 percent shareholders, directors, and officers—as there is in the 1934 Act. Likewise, the Venezuelan law does not provide for the return of "insider" profits to the company. If any "insider" trading activities were to be discovered, it would probably have to be done on the basis of compiling the registration data submitted to the CNV under Articles 20[179] and 112.[180] However, since most of this information is to be reported on an annual basis, it would be of little use in detecting "insider" activities. Also, even if "insider" trading was discovered, there are no express administrative or penal sanctions to remedy the problem. The silence of the Venezuelan Capital Markets Law in this regard is troublesome, since one of the major criticisms of the securities markets prior to 1973 was that there did not exist any legal prohibition against using inside information in securities transactions.[181] Although specific examples were not cited in the Deltec report, it was noted that there were many notorious abuses in this respect.[182]

Significantly, it is noted that certain existing provisions of the Venezuelan law might be utilized to safeguard shareholder rights. Article 266 of the Venezuelan Commercial Code[183] deals with the liability of corporate directors to shareholders. A leading Venezuelan jurist's interpretation of this provision

[177] *Id.*
[178] *Id.*
[179] 1973 Law, art. 20, at 3-4.
[180] *Id.* art. 112, at 12.
[181] CEMLA, at 23.
[182] *Id.*
[183] CODIGO DE COMERCIO, art. 266, at 301.

indicates that a person who has purchased company shares based upon false or exaggerated information provided by a director has a right to recover damages against such wrong-doing director.[184] Article 370 of the Venezuelan Commercial Code also establishes liability for anyone who acts fraudulently by means of forgery, false public statements, or other falsehoods, with the desire to obtain or intent to obtain shares or bonds.[185] Query: do these two provisions include within the scope of their coverage the "omission" of a material fact? Do these provisions have scienter requirements such that the plaintiff must show that the defendant acted with the intent to deceive, manipulate, or defraud? Is there a requirement that the plaintiff show that in some way he relied upon the defendant's misrepresentation or nondisclosure?

Possible use of the Venezuelan Commercial Code by a shareholder certainly raises the question of when and to what type of transactions the code applies. Also, will the Commercial Code apply if the shareholder bringing the action is not a merchant? This latter question arises in cases of "mixed" transactions where the transaction is commercial for one party (e.g., the director or the company) but not for the other party (e.g., the shareholder). Under the broad scope of Articles 1[186] and 2[187] of the Venezuelan Commercial Code, many "mixed" transactions are brought within the sweep of the Commercial Code. This is based upon the code's emphasis on the "mercantile act," as opposed to being solely on a person's as a "merchant."[188] The Commercial Code's definitions of "mercantile acts" consist of lengthy and unsystematic enumerations.[189] The primary influence for this "mixed transaction" approach of the Venezuelan Commercial Code can be traced to the French Commercial Code model.[190,191] In response to the initial inquiries, then, it would appear that a shareholder would not be precluded from bringing an action under provisions of the Venezuelan Commercial Code. However, it is noted that one problem with the "mixed transaction" approach is that it often results in frustrating the protective purpose of a Civil Code provision and in oppression of the weaker party.[192]

An injured shareholder can also seek judicial relief by utilizing the Venezuelan Civil Code. Article 1.185[193] of the code provides that anyone who

[184]J. Arismendi, Tratado de las Sociedades Civiles y Mercantiles, § 392, at 339 (2d ed. 1949).

[185]Codigo de Comercio, art. 370, at 414.

[186]*Id.* art. 1, at 39.

[187]*Id.* art. 2, at 39-61.

[188]*Id.* art. 1, at 39.

[189]*Id.* art. 2, at 39-61.

[190]R. Schlesinger, Comparative Law 404-09 (1970).

[191]J. Arismendi, Tratado de las Sociedades Civiles y Mercantiles 17 (2d ed. 1949).

[192]R. Schlesinger, Comparative Law 408(1970).

[193]O. Lazo, Codigo Civil de la Republica de Venezuela, art. 1.185, at 601-03 (1962).

with intent, or through negligence or imprudence, has caused injury to another, is obligated to repair such injury. Two independent sources indicate that this provision would be especially suited to a situation involving use of manipulative or deceptive devices or an untrue statement or omission of a material fact by a director or company. According to Professor Arismendi's analysis, this provision covers omissions or the giving of false information to the public.[194] A second interpretation supports this position by analogy to the corresponding French Civil Code provision. According to Professor Yates, Article 1.382[195] of the French Civil Code would implicitly include within its coverage omission of a material fact (e.g., possible impact on a merger transaction of an unfavorable decision in pending litigation).[196]

The Venezuelan Penal Code also provides possible remedies for an injured shareholder. Article 444[197] of the code deals with fraud and specifically includes within its coverage corporate directors. The scope of the provision is quite broad: anyone who uses any means of deceit to obtain for himself or others some gain or unjust profit with detriment to another is subject to a prison sentence of from six to thirty months.[198] Query: would this provision also include omissions of material facts which prove injurious to shareholders? Two factors seem to work against this provision previously having been an effective shareholder's protective device. First, any action brought under this Article would apparently have to be brought by an individual without the assistance of the state. Elements working against widespread investor reliance upon this device are common to many legal systems—burdensome litigation expenses, court delay, and judicial inexperience in this field. Second, this Article's burden of proof, much like the state statutes which allow common law actions in the United States prior to the federal securities legislation of 1933 and 1934, is rather stringent in that it does require a showing of scienter or criminal intent.

A third significant provision of the Securities Exchange Act of 1934 dealt with Section 14 and the regulation of proxies.[199] The importance of the regulation of proxies was aptly noted by Professor Loss: "The proxy rules are very likely the most effective disclosure device in the SEC scheme of things. The proxy literature, unlike the application for registration and the statutory

[194] J. ARISMENDI, TRATADO DE LAS SOCIEDADES CIVILES Y MERCANTILES, § 390, at 338 (2d ed. 1949).

[195] E. WRIGHT, THE FRENCH CIVIL CODE, art. 1.382, at 256 (1908).

[196] Yates, *Substantive Law Aspects of Enforcement of Foreign Judgments Between Foreigners in France: The Competence Question*, 9 INT'L LAW. 267-68 (April 1975).

[197] *Leyes y Decretos de los Estados Unidos de Venezuela*, Tomo V, CODIGO PENAL, art. 444, at 628 (1943).

[198] *Id.*

[199] 15 U.S.C. § 78n (1970).

reports, gets into the hands of investors. Unlike the [1933] Securities Act prospectus, it gets there in time. It is more readable than any of these other documents and it gets to a good number of people who never see a prospectus."[200]

Two additional factors underscore the importance of proxies. First, they are an effective device for perpetuating existing management and its policies. Second, they provide management with essentially a free rein to say whatever it desires in any proxy solicitation campaign.

In another article dealing with proxy contests, it was noted that the proxy rules provide a three-level approach to the voting problems of the shareholder. First, the shareholder has the opportunity to solicit proxies from fellow shareholders, and to force the management to include in its proxy statement shareholder proposals. Second, the rules require full disclosure of all material pertinent to proposals for corporate action submitted by the management to shareholders by means of proxies. Third, the use of fraud in the solicitation of proxies is made unlawful.[201]

Unlike the 1933 Act, the Venezuelan Capital Markets Law does not address the issue of regulation of proxies. In addition, the Venezuelan Commercial Code makes only one specific reference to proxies, whereby it prohibits directors, managers and comisarios from serving as proxies at shareholder meetings.[202] A study of the Venezuelan stock exchanges conducted in the mid 1960s indicates that there does exist a proxy system whereby a shareholder may authorize another person to attend a meeting and vote.[203] This study noted that the proxies are frequently solicited by corporate management.[204] In view of the above-mentioned importance of proxy solicitation, it is difficult to understand why this vital area was left untouched by the Capital Markets Law.

Intermediate Financial Institutions

As was noted previously, there are a number of prerequisites which are necessary for the finance system to work effectively as a method of generating savings. One of these prerequisites is that intermediate financial institutions such as banks, stock exchanges and mutual funds exist so as to collect and channel into productive investments those funds which the working and investing population has saved. The only intermediate financial institutions which the Venezuelan Capital Markets Law specifically regulates are stock ex-

[200]L. LOSS, SECURITIES REGULATION 1027 (2d ed. 1961).
[201]Emerson and Latcham, *Proxy Contest Expenses in Shareholder Democracy*, 4 W. RES. L. REV. 5, at 7 (1953).
[202]CODIGO DE COMERCIO, art. 285, at 318.
[203]D. EITEMAN, STOCK EXCHANGES IN LATIN AMERICA 59 (1966).
[204]*Id.*

changes,[205] brokers,[206] transfer agents,[207] and mutual funds.[208] The author notes that the law does not regulate underwriters, banks, pension funds, union funds, or insurance companies.

A significant part of the law provides for a fairly extensive regulation of stock exchanges. Effective regulation in this area was definitely needed since the exchanges were essentially unregulated prior to 1973.[209] In large part this was due to the fact that the exchanges never applied disciplinary measures against any of their members or revoked any company's listing if it violated the exchange's regulations.[210]

Under Article 78 of the Capital Markets Law each securities exchange is constituted as a corporation.[211] The management of the exchange is structured in such a manner that it is under the control of the brokers.[212] Although the exchanges are self-regulating, all of their rules governing their conduct and operations must be approved by the CNV.[213] The exchanges are also subject to the disclosure requirements of the law and must permit inspection of their books by the CNV.[214]

In addition, the activities of brokers are regulated, and violators of the rules are subject to expulsion or suspension from the exchange.[215] Of special interest is the prohibition against fixing securities prices or altering the free play of supply and demand in any way.[216] Query: exactly what type of activity would unlawfully alter the free play of supply and demand? Would a broker owning substantial shares of stock in one company be prohibited from "dumping" these shares on the market and thereby causing the market price of the stock to be depressed?

A major purpose in regulating the securities exchanges was to specifically limit the number of exchanges.[217] Under the law, each city is allowed only one securities exchange.[218] This provision was apparently aimed at forcing the merger of the country's two existing exchanges—the Caracas and the Miranda exchanges. The merger effort was completed in 1974, when a fifty-seat ex-

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[205] 1973 Law, arts. 78-103, at 8-11.
[206] *Id.*
[207] *Id.* arts. 104-110, at 11.
[208] *Id.* arts. 62-77, at 7-8.
[209] CEMLA, at 89,96.
[210] *Id.* at 92.
[211] 1973 Law, art. 78, at 8.
[212] *Id.* art. 83, at 9.
[213] *Id.* art. 81, at 8-9.
[214] *Id.* art. 86, at 9.
[215] *Id.* arts. 88,90, at 9-10.
[216] *Id.* art. 101, at 10.
[217] *Id.* art. 79, at 8.
[218] *Id.*

change located in Caracas began to function.[219] The overriding practical consideration in this instance was that the actual volume of transactions previously was not sufficient to adequately support financially brokers of both the competing exchanges.[220] As such, prior to 1973 many brokers dealt in securities transactions only on a part-time basis and could hardly have been considered professionals.[221]

A significant aspect of limiting each city to only one stock exchange is that the government has created a monopoly of sorts. Brokerage fees are now regulated and approved by the CNV,[222] as are all the major functions and duties of the exchanges.[223]

In regard to the securities exchanges, the Capital Markets Law overlooked two important problem areas. First, the law did not specifically prohibit over-the-counter securities transactions. As a result, a parallel market will be permitted to compete with the officially sanctioned Caracas exchange. This was a problem prior to 1973, since it deprived the organized exchanges of valuable commissions.[224]

The law was also deficient in terms of not specifically regulating underwriters. As Professor Roth noted in his article dealing with the Brazilian and Israeli markets, legal prerequisites of competence and financial responsibility and established standards of conduct are vital in a system based on disclosure, whereby the lay investor is by necessity almost forced to rely on these people when dealing in the complicated matters of securities investment.[225]

One possible remedy for this defect in the law is to expressly require that any issue of securities may be offered only through a qualified intermediary.[226] Additionally, there could be a requirement that underwriters register with the CNV and comply with certain requirements as to capitalization, commissions, professional conduct, and technical competence.[227]

Prior to the Capital Markets Law the process of transferring shares was neither easy nor rapid, and resulted in the liquidity of the market being impeded.[228] In order to alleviate this problem, and to establish norms of conduct, the law expressly regulates transfer agents.[229] These agents, generally

[219] 8 BANK OF LONDON & SOUTH AMERICA REPORT 439 (July 1974).
[220] CEMLA, at 91.
[221] *Id.*
[222] 1973 Law, art. 81, § 6, at 8.
[223] *Id.* arts. 78-103, at 8-11.
[224] A. BASCH & M. KYBAL, CAPITAL MARKETS IN LATIN AMERICA 65 (1970).
[225] Roth, *Capital Market Development in Israel and Brazil: Two Examples of the Role of Law in Development*, 19 STAN. L. REV. 1296 (1967).
[226] *Id.* 1296-97.
[227] *Id.*
[228] CEMLA, at 52.
[229] 1973 Law, arts. 104-110, at 11.

banks, are retained by a company with widely traded securities for the purpose of managing stock ownership transfers and mailing dividend and interest checks. The agent issues new certificates upon the surrender of the old ones and maintains the current list of security holders. Prior to any transfer, the agent requires appropriate documentation of the right to transfer the securities.[230] Unlike previously, where transfer delays of months were common, the transfer agents are now required to complete the process within 20 days after the stockholder makes his request. In order to safeguard investors against fraud or incompetence, transfer agents are liable for damages suffered by investors.[231]

Efforts to strengthen the secondary market have moved beyond the regulatory provisions of the Capital Markets Law, and have resulted in the creation of two new intermediate financial institutions. Significantly, these institutions are not provided for in the Capital Markets Law, but rather have been created to facilitate the development of an effective and integrated primary and secondary market. The first institution, Sociedad Financiera Valinvenca, began operations at the beginning of 1975. A *sociedad financiera* is technically a private development bank. It is also referred to as a finance company. This type of institution is a combination of private development bank, investment bank and trust company. Financieras are authorized to receive time deposits and to issue their own bonds of up to ten years' maturity. This type of institution was originally organized in Mexico in the 1920s, and has been legally authorized in Venezuela since 1961.[232] In Venezuela there are currently twenty-six *financieras*, and most of them have tended to concentrate on consumer financing of durable goods. Since 1975, *financieras* in Venezuela have been authorized to invest unlimited amounts in corporate equity and to underwrite new equity issues.[233]

Sociedad Financiera Valinvenca, a private company, grew out of a planning study conducted by the Venezuelan Minister of Finance and the International Finance Corporation (IFC) in 1971. Equity investors in Valinvenca (total paid-in capital of $2.3 million) include IFC (15 percent equity investment), J.P. Morgan Overseas Capital Corporation (20 percent equity investment), Inversiones Finalven, S.A. (Venezuela's largest financiera; 35 percent equity investment); and the Banco Provincial (15 percent equity investment). Valinvenca's basic purpose is to facilitate development of the primary market for securities, and to aid in development of a commercial paper market. In this role Valinvenca is intended to act as a broker-dealer in the money market, and

[230] D. VAGTS, BASIC CORPORATE LAW 950 (1973).
[231] 1973 Law, art. 109, at 11.
[232] A. BASCH & KYBAL, CAPITAL MARKETS IN LATIN AMERICA 53-55,151 (1970).
[233] INVESTING, LICENSING, AND TRADING CONDITIONS ABROAD—Venezuela, Aug. 1975, at 18-19.

as an underwriter of long-term debt and equity. Valinvenca's initial activity has been in the money market, where it has issued certificates of deposit and acted as a paying agent in the placement of commercial paper. When the long-term capital markets have become sufficiently developed, it is anticipated that Valinvenca will begin to distribute debt and equity issues on either a best-efforts or underwritten basis.[234,235] Due to the limited amount of information available on the activities of this new financial institution, the author is unable to explain in any greater detail how these issues will be distributed.

The second new financial institution, Sociedad Financiera Promotora del Mercado de Capitales (PROMECA), was established in 1975. PROMECA, a joint public-private venture, also grew out of the 1971 planning study conducted by the Venezuelan Minister of Finance and the IFC. Equity investors in PROMECA (initial paid-in capital of $4.7 million) include the Banco Industrial de Venezuela (a state-owned development bank; 15 percent equity investment), IFC (15 percent equity investment), and an additional group of 66 local private investors (including thirteen commercial banks, fifteen *financieras*, and thirty insurance companies). PROMECA's basic purpose is to serve as a specialized secondary market liquidity agency and as a market for long-term debentures issued by industrial firms and financieras.[236,237]

New Techniques To Promote Investment

The Venezuelan Capital Markets Law was especially innovative in establishing new instruments and devices to encourage investment. An important example of this innovative effort was the provision expressly permitting the issuance of convertible debentures. These instruments did not exist in Venezuela prior to 1973.[238,239] There was no express legal prohibition against convertible debentures, rather companies were prohibited from having shares authorized prior to subscription.[240,241,242]

The dual role which this type of security can serve apparently convinced legislators of its utility. In the case of Venezuela, where so many companies are closely held, the convertibility feature serves an important function for both companies and investors. In the early stages of a company's history, when it is

[234]*Id.*

[235]FINANCING FOREIGN OPERATIONS—Venezuela, Dec. 1975, at 941-42.

[236]*Id.*

[237]INVESTING, LICENSING, AND TRADING CONDITIONS ABROAD—Venezuela, Aug. 1975, at 18-19.

[238]CEMLA, at 22.

[239]A. HERNANDEZ, ALGUNOS ASPECTOS DEL REGIMEN DE LA OFERTA PUBLICA DE TITULOS-VALORES EN VENEZUELA 136-37 (1973).

[240]*Id.*

[241]CODIGO DE COMERCIO, art. 249, at 296.

[242]R. LOMBARD, AMERICAN-VENEZUELAN PRIVATE INTERNATIONAL LAW, fn. 304, at 77 (1965).

necessary to raise capital, an investor may be unwilling to accept stock alone for his contribution and may insist upon the protection of a debt claim. At the same time, he is probably not satisfied with just a high interest rate as an adequate return for the risk involved. In this context the convertible debenture is designed to serve the needs and desires of both the company and the investor—it affords the investor and the company the flexibility which fledgling new businesses must provide in order to attract needed financing.[243,244]

In order to further encourage public investor acceptance of convertible debentures, special safeguards are provided by the law.[245] Primary among these is the required election of a bondholder representative to look after the interests of the bondholders. Initially, this representative is to be appointed by the company, subject to approval by the CNV. The provisional representative is subsequently to be replaced in an election whereby a new bondholder representative—possibly a bank, financiera, or insurance company—will be selected by a majority of the bondholders.[246] The law is somewhat vague in this area, since it does not indicate how soon the election must take place. In this subsequent election the company apparently has no vote.

A second means whereby the Venezuelan Capital Markets Law was intended to facilitate flexibility in financing corporate investment and expansion was through the creation of an entirely new corporate form, the "authorized capital" corporation (*sociedad anonima de capital autorizado* or SACA).[247] Stock companies with a subscribed capital in excess of one million bolivars are able to adopt the SACA form.[248] Once this form is adopted, company shareholders may authorize the directors to increase the company's capital stock to a specific amount through the issuance of new shares.[249] The key feature and advantage to the SACA corporate form is that it enables the directors to increase the company's capital anytime within a two-year period from the date of shareholder authorization.[250] Previously, it was much more difficult and time-consuming for a company to increase its capital stock. Article 280 of the Commercial Code required that any increase in capital stock had to be voted on at a shareholders' meeting, with at least three-fourths of the shareholders present. A favorable vote of at least half of the shareholders was then necessary to approve the increase.[251]

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[243]W. CARY, CORPORATIONS 1241 (1969).
[244]Nunez, *De los Titulos Valores Emitidos por las Sociedades Anonimas*, 41 U. DEL ZULIA 61-63 (1974).
[245]1973 Law, arts. 36-44, at 5-6.
[246]*Id.* art. 36, at 5.
[247]*Id.* arts. 48-55, at 6.
[248]*Id.* art. 48, at 6.
[249]*Id.* art. 51, at 6.
[250]*Id.* art. 52, at 6.
[251]CODIGO DE COMERCIO, art. 280, at 317.

One major aim of the Venezuelan Capital Markets Law was to broaden the ownership of securities in the country. One means to achieve this goal was to create mutual funds.[252] In Venezuela, prior to 1973, no open-end[253] mutual funds existed due to the prohibition against a company having variable capital.[254] Article 299 of the Commercial Code required that shares could not be fractional and that they must be whole and indivisible.[255,256] The prohibition against fractional shares was not removed by the Capital Markets Law; rather, it simply provided that there would henceforth be mutual funds.[257]

Based upon the experience of the more developed countries, however, it was apparent that widespread investor participation in mutual funds and other similar institutional type investors could be a crucial factor in successfully developing the capital markets.[258] The role played by mutual funds in the United States seems to indicate that they would be well-suited for the Venezuelan market. Basically, such companies pool the funds of investors, which are obtained through the sale of shares and bonds, in a portfolio of securities. The portfolio is specially designed and managed to obtain for shareholders the benefits of diversification, professional selection and supervision of securities, and skilled timing of purchases and sales. The idea is that a shareholder, with a relatively small outlay per share, is able to attain results superior to those he could obtain through direct investment. In view of the government's desire to attract large numbers of new and unsophisticated investors, it is clear that the mutual fund was an attractive and potentially profitable mechanism. The mutual funds, given their traditional role in the United States of funneling savings into outstanding securities in the secondary markets rather than financing new capital investment, offered the real possibility of strengthening the weak secondary securities market in Venezuela. As was noted previously, the traditional weakness of the secondary market in Venezuela was one major factor in discouraging public investor participation. There is no indication in the Capital Markets Law whether these organizations are exempt from corporate tax as in the United States.

A second means whereby the Capital Markets Law encouraged a wider ownership of securities was through the creation of a new corporate form, the

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[252] 1973 Law, arts. 62-77, at 7-8.

[253] In an open-end mutual fund the shareholders and capital are variable since the shares are redeemable; in contrast are closed-end mutual funds, which have a fixed capital and unredeemable shares. A. BASCH & M. KYBAL, CAPITAL MARKETS IN LATIN AMERICA 57 (1970).

[254] *Id.* 58.

[255] CODIGO DE COMERCIO, art. 299, at 351.

[256] J. ARISMENDI, TRATADO DE LAS SOCIEDADES CIVILES Y MERCANTILES, § 465, at 403-04 (2d. ed. 1949).

[257] 1973 Law, arts. 62-77, at 7-8.

[258] H. DOUGALL, CAPITAL MARKETS AND INSTITUTIONS 78-85 (1970).

"open capital corporation" (*sociedad anonima inscrita de capital abierto* or SAICA).[259] The underlying policy consideration in this regard was to encourage closely held companies to place a large part of their capital stock in the hands of many different investors. The SAICA concept was a deliberate attempt to foster the "democratization" (i.e., wider public ownership) of capital in Venezuela.[260]

Initially, a major obstacle for companies to qualify as SAICAs was the requirement of having 50 percent of the company shares distributed among at least 50 shareholders for each one million bolivars of paid-in capital.[261] However, this requirement was simply too unrealistic given the then-existing corporate structure. At that time the country's most widely held company, Electricidad de Caracas, had only 8,000 shareholders.[262] As a result, this provision was reformed in 1975.[263] The new provision requires that a SAICA distribute 50 percent of its shares to the public, but now leaves open the required number of shareholders and the maximum size of holding.[264] Query: does this provision defeat the entire goal of encouraging widespread public ownership of shares via SAICAs?

The first step in the SAICA campaign centered around special measures designed to protect minority shareholders and thereby increase public investor confidence in shareholding. Specific measures provided for minority shareholder participation in the election of the board of directors.[265] The law is not clear as to exactly how the election of the board will take place. However, the importance of the provision is that it requires that those shareholders who participate in the election of a majority of the board of directors (a minimum of five who will hold office for one-year terms) of the SAICA corporation thereafter cannot participate in the election of the remaining board members who represent the minority.[266] Although it is not specifically designated as cumulative voting, this provision seems to amount to a type of cumulative voting in that it guarantees some minority representation on the board. Query: how, when, and by whom is it to be determined exactly how many members there will be on the board?

Equally important for minority shareholders is their right to participate in

[259]1973 Law, arts. 56-61, at 6-7.

[260]Calatchi, *Venezuela's Capital Markets Take on an International Flavour*, EUROMONEY, Dec. 1976, at 55-56.

[261]1973 Law, art. 56, § 3, at 6-7.

[262]The author notes that there is no information readily available as to how many shares or what type.

[263]Decree 882, 394 (Supp.) Gaceta Legal, art. 60, § 2, at 51, May 31, 1974.

[264]*Id.*

[265]1973 Law, art. 123, at 13.

[266]*Id.*

the election of two comisarios.[267] Pursuant to Article 125, each comisario is to be elected separately, with each shareholder allowed to vote only once, unless the vote is unanimous.[268] Unfortunately, the provision is somewhat vague in that there is a question as to whether the comisario election provision applies only to SAICAs or to all companies under the control of the CNV. In view of Señor Diaz' experience with the comisarios of CATC, it is apparent that major changes have been made in the election of these officials. Previously, they were elected at the annual shareholders' meeting by a majority of the shareholders.[269] Also, previously no limitation was placed on the relationship of the board and comisarios.[270] Article 125 changed this latter aspect, since it prohibited comisarios from being either agents of the directors, employees of the company, or relatives of the directors.[271] Query: will these new safeguards now prevent the comisarios from being a mere puppet of the directors? Will the comisarios now effectively safeguard minority shareholder rights?

Another innovation in terms of minority shareholder protection is the requirement that a company distribute 50 percent of its net after-tax profits annually, with at least 25 percent of this amount being paid in cash.[272] This provision is important for two reasons. First, the dividend requirement applies not only to SAICAs, but to any company making a public offering. Second, this cash dividend policy could adversely affect a company's expansionary program by forcing it to pay out sorely needed capital. Query: to what extent will this requirement have an adverse impact upon national development by reducing the amount of valuable operating capital available to a company? Certainly such a change is drastic and clearly runs counter to the traditional practice and desire of closely held companies to not share profits with outside elements.

Tax incentives are the primary inducements offered to companies to adopt the SAICA form. Originally, the law allowed the national executive to grant tax exemptions up to a maximum of ten years.[273] The exemption offered to the SAICA companies was based on the percentage of stock in the hands of the public. The maximum exemption available was 15 percent of the tax payable on the total net income of the company.[274]

Tax exemptions existed for shareholders who purchased SAICA stock. Article 131 provided that there was no tax on interest or dividends [from SAICA

[267]*Id.* art. 125, at 13.
[268]*Id.*
[269]CODIGO DE COMERCIO, art. 287, at 319.
[270]*Id.* art. 309, at 363.
[271]1973 Law, art. 125, at 13.
[272]*Id.* art. 127, at 13.
[273]*Id.* art. 132, at 13.
[274]*Id.* art. 130, at 13.

stock], and capital gains would also be tax-exempt if they were reinvested in SAICA securities.[275]

Not totally unexpectedly however, the tax incentives were not considered to be adequate[276] and resulted in not one company adopting the SAICA form. A number of different factors can be identified as contributing to the failure of this part of the 1973 law. The scope of the original law was rather limited in that it allowed only tax exemptions and made no provision whatsoever for any tax deductions.[277] Tax exemptions have little effect on a company unless it is already generating sizable corporate profits.[278]

In regard to investors, a tax deduction could have acted as an added incentive to them to acquire securities. An example of this is if the 1973 Venezuelan Capital Markets Law would have allowed taxpayers to deduct from gross income a certain percentage of money spent acquiring SAICA shares. The effect of the deduction would have been to lower the purchase price of the security and thereby increase its effective yield.[279]

Tax incentives such as exemptions and deductions can be classified as "marginal" incentives.[280] They operate to change the marginal profitability of a business venture or the effective yield of a security. However, they influence decision-making only if economic units—both companies and individuals—have already calculated the profit potential in a situation, and are prepared to change their investment decisions based on the marginal difference created by the incentive.[281] Obviously, the incentives offered by the 1973 Capital Markets Law were not sufficiently strong by themselves to change past patterns of behavior. Closely held corporate enterprises could not be induced to voluntarily change their traditional policies and beliefs, and wary investors could not be induced to discard their fear of investing in company shares.

In large part it was the above-mentioned factors which led to the 1975 revised Capital Markets Law.[282] The 1975 reform version was basically directed at rectifying the deficiencies in the tax incentives originally offered. The scope of the new law was quite limited however, since it was specifically aimed at inducing companies to convert to SAICA form.[283] In order to effectuate the new

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[275]*Id.* art. 131, at 13.

[276]*Venezuelan Capital Markets Law Offers Only Sketchy Incentives*, BUSINESS LATIN AMERICA, March 1, 1973, at 71-72.

[277]*Venezuela Proposes Personal Tax Breaks to Stimulate Growth of Capital Market*, BUSINESS LATIN AMERICA, April 22, 1971, at 123,125.

[278]D. TRUBEK, LAW, PLANNING AND DEVELOPMENT OF THE BRAZILIAN CAPITAL MARKET 34 (Bull. Nos. 72-73, April 1971).

[279]*Id.*

[280]*Id.*

[281]*Id.*

[282]Decree 882, 394 (Supp.) Gaceta Legal 46-59, May 31, 1974.

[283]*Id.* art. 130, at 57.

law the national executive was given a broad grant of power to decree various tax incentives, including tax exemptions.[284] The national executive subsequently decreed new tax exemptions which are considerably more generous than those offered by the 1973 law.[285] Currently, companies that distribute a minimum 50 percent of their shares to the public are eligible for a 25 percent exemption from corporate income tax. If 50-60 percent of the shares are distributed to the public, then the exemption is 30 percent. If 60-75 percent or more of the shares are publicly held, then the exemption is 40 percent. If 75 percent or more of the shares are publicly held, then the exemption reaches 50 percent.[286]

Due to the lack of current information, it is difficult to accurately assess whether these new incentives will be more successful than the original ones. To date there are five SAICAs.[287] One of the SAICAs, Industrias Berol, opted for this corporate form for the purpose of complying with the divestment requirements of the Andean Foreign Investment Code.[288] The remaining companies—Telares de Palo Grande, Sociedad Financiera de Venezuela, and Banco Provincial—have all apparently opted for the tax exemptions since they are national companies and are not subject to the Andean Foreign Investment Code's divestment requirements.[289]

Conclusion and Recommendations

There is little doubt that fundamental obstacles continued to impede the growth and development of the capital market in Venezuela in the period from 1973-76. Investors were still wary of entering the market, companies were hesitant to open up and "go public," vital links in the intermediate financial structure remained underdeveloped, and the supply and quality of skills needed to operate such a system were limited. A consideration of selected basic data over the three-year period in which the Capital Markets Law has been in effect highlights some of the continuing weaknesses. In 1974, 1.3 billion bolivars worth of securities were traded on the Caracas stock exchange. Of this total, bonds accounted for 58 percent, while equity securities accounted for only 12 percent. The remaining 30 percent represented foreign exchange trading.[290] In May of 1975 bonds accounted for over 60 percent of the securities transactions, with stocks representing 25 percent of the total.[291] Clearly, there has

[284] *Id.*
[285] INVESTING, LICENSING, AND TRADING CONDITIONS ABROAD—Venezuela, Aug. 1975, at 18-19.
[286] *Id.*
[287] Bolin, *Investment Climate Improving, Stock Market Shows Signs of Life*, Daily Journal [Ven], Feb. 28, 1977, at 26, col. 3.
[288] *Id.*
[289] *Id.*
[290] FINANCING FOREIGN OPERATIONS—Venezuela, Dec. 1975, at 941.
[291] *Id.*

been some increased activity on the exchange in terms of equity security transactions. However, it is important to note that the 13 percent increase in the trading of equity securities was probably somewhat deceptive, since in fact the activities of the "Caracas" exchange in 1975 were bolstered following its merger with the Miranda exchange.

The latter part of 1975 did see some improvements in the public offering of equity securities. Private companies placed a total of eight registered equity issues, all with prospectus. These equity issues amounted to 332 million bolivars ($77 million). However, the market still remains quite thin. At the end of 1975, only seventy-four companies were registered with the CNV.[292] Of the seventy-four registered companies, the shares of twenty-nine of them were never traded in 1975,[293] and only twelve out of the total seventy-four were traded on a regular basis.[294]

Indications are that there continues to be a shortage of private sector equity funds for new ventures. A major contributing factor to this problem is the attraction for investors of bonds which currently pay 8 percent tax-free interest.[295] This continuing investor preference for fixed-income securities is part of a trend which apparently began following the 1958-63 Venezuelan financial crisis,[296] and has remained fairly constant since then. Preference for this type of security, as contrasted with common stocks, has been due to a number of factors. First, an important degree of liquidity is guaranteed bondholders by the open market buying operations of the central bank in government bonds and by the stabilizing operations of the Central Hipotecaria in the case of mortgage bonds.[297] Second, the net yields on fixed-income securities have generally compared very favorably with the return on common stocks.[298]

In looking toward the future the main question is what can be done to achieve a more viable capital market? The possibilities are many, and certainly there is room left for improvement. Any consideration will center around the divestment requirements imposed upon companies in Venezuela by the Andean Foreign Investment Code. Representatives of all groups—government, business, and academic—have previously stated their belief that the divestment program and a vigorous capital market program go hand-in-hand. The results to date, however, have not been very encouraging. As of January, 1977 there are indications that only one such public underwriting—involving

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[292] Bolin, *Investment Climate Improving, Stock Market Shows Signs of Life*, Daily Journal [Ven], Feb. 28, 1977, at 26, col. 1.

[293] *Id.*

[294] *Id.*

[295] Calatchi, *Venezuela's Capital Markets Take on an International Flavour*, EUROMONEY, Dec. 1976, at 54.

[296] M. HASSAN, ECONOMIC GROWTH AND EMPLOYMENT PROBLEMS IN VENEZUELA, 26-31 (1975).

[297] A. BASCH & M. KYBAL, CAPITAL MARKETS IN LATIN AMERICA, 153-54 (1970).

[298] *Id.*

Industrias Berol, with a public offering of 296, 800 common shares at twenty bolivars per share—has occurred.[299,300]

Far more unsettling, however, has been the recent change of events in Venezuela regarding Decree 62—Venezuela's legislative implementation of the Andean Foreign Investment Code.[301] Recent reports indicate that Decree 2031 of February 8, 1977 replaces Decree 62.[302] Significantly, the new law provides for extensive exemptions from the divestment deadlines. In some instances these dates have been extended from the original target date of May 1977 until February 1980. Further, the Agency of Foreign Investment (SIEX) of Venezuela has been given the authority to extend for an undetermined time the divestment period for a company due to "special circumstances." Such cases are to be determined on a case-by-case basis. Query: what must a company do in order to show "special circumstances?"

Three factors contributed to this situation. First, many companies have encountered difficulties in finding buyers. Second, in many of those cases in which companies found buyers the government has apparently refused to authorize the arrangements. The government's actions here are a result of its desire to ensure a more equitable distribution of wealth among individual investors and to prevent any further concentration of power in the traditional industrial groups. Third, private sector business interests have pressed the government since 1973 to adopt what they believe to be a less stringent and more realistic approach to foreign investment.[303]

Although it is too early to fully assess the results of this new legislative reform, it would appear that the immediate result will be to slow down the divestment process. Given the prior assumption that the foreign investment code's divestment requirements would stimulate the growth of the capital market, it is now possible that growth in the market will take place at a slower rate. There is little doubt that this is an immediate problem which could have a severely adverse impact on the development of the market.

The extent to which the market will now grow is much more dependent on factors other than the divestment program. The Venezuelan capital markets program obviously faces a critical stage of development. Brazil, in the period from 1966-67, when faced with a crisis of a different nature but of equally important dimensions, opted for a system of forced savings tax incentives to

[299]Bolin, *Investment Climate Improving, Stock Market Shows Signs of Life*, Daily Journal [Ven], Feb. 28, 1977, at 26, col. 5.

[300]The underwriter was Sociedad Financiera Promotora del Mercado de Capitales, C.A., of Caracas.

[301]Decree 62, 13 INT'L LEGAL MAT'LS 1220-21 (1974).

[302]*New Decree Shows Changes in Attitudes toward Foreign Investors*, BUSINESS LATIN AMERICA, March 9, 1977, at 75, 78-79.

[303]*Id.*

stimulate a weak and faltering market.[304] The question now is how innovative Venezuelan planners will be in coping with the new problem situation.

Certainly a possible remedy includes consideration of Brazil's solution to its problem—Decree Law 157.[305] Pursuant to this legal device, an individual taxpayer was allowed to credit against his income tax that money which he invested in authorized financial institutions. In turn, these institutions then reinvested the DL 157 funds in the shares or debentures of private firms which had been approved by the Central Bank of Brazil. The DL 157 credit was limited to 12 percent of the tax due. In order to qualify for the credit, the taxpayer would have to hold the DL 157 shares in the authorized financial institution for at least four years.[306]

The effective operation of a tax incentive such as DL 157 requires two preconditions. First, there must be a broadly based tax at rates high enough to encourage a significant number of people to seek the tax relief. Second, there must be a tax administration system capable of collecting taxes and enforcing penalties for tax evasion.[307] In the case of Venezuela—unlike Brazil—these two preconditions are not present. Until these are fulfilled, it is difficult to envisage any tax incentive effectively spurring the growth of the capital markets by inducing greater participation by privately held companies and public investors.

Traditionally, the petroleum sector's taxes have constituted the bulk of total government revenues. In 1977 petroleum is expected to contribute approximately 80 percent of the government's tax revenue.[308] In contrast, the nonpetroleum [private sector] taxes constituted only 9 percent of the government's total revenue in 1974.[309] Under the current progressive corporate tax structure (referred to as "schedule A") the corporate tax rate ranges from 15 percent on corporate income of 100,000 bolivars or less, and continues up to 50 percent on corporate income of 28 million bolivars or more.[310] Although there is a progressive individual income tax (referred to as "schedule C") its contribution to the government's total revenue is also negligible when compared to the petroleum sector. Administration of the tax laws leaves much to be desired. Tax evasion—by both companies and individuals—is common.

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[304]D. TRUBEK, LAW, PLANNING AND DEVELOPMENT OF THE BRAZILIAN CAPITAL MARKET, (Bull. Nos. 72-73, April 1971) at 45-71.

[305]Art. 3 [1967] 1 Colecao (legis.) 177, D.O., Feb. 13, 1967.

[306]Carl, *The Brazilian Experiment in the Creation of an Aircraft Industry*, 38 J. AIR L. & COMM. 41-42 (1972).

[307]*Id.*

[308]*Venezuela's Proposed Tax Reform and 1977 Budget Are Strongly Criticized*, BUSINESS LATIN AMERICA, Nov. 22, 1976, at 373-74.

[309]*Venezuelan Businessmen Speak Out Strongly Against Proposed Tax Reform*, BUSINESS LATIN AMERICA, Jan. 5, 1977, at 6-7.

[310]*Id.*

Some estimates indicate that under the current system tax evasion runs as high as 3 billion bolivars per year.[311] Although nonpayment of taxes is supposedly an offense punishable by imprisonment and fines, such penalties are seldom imposed.[312]

The absence of an effective taxation system in Venezuela would obviously preclude adoption of a DL 157 type device. A solution to this problem might be found in President Perez' current push for massive tax reform.[313] The new tax plan would focus on three goals: (1) increase private sector corporate taxes, such that tax rates would range from 18 percent on corporate income of 100,000 bolivars or less, and continue up to 55 percent on corporate income of 6 million bolivars or more; (2) increase personal income tax for individuals earning over 200,000 bolivars per year; (3) correct the country's history of tax evasion by actively punishing nonpayment of taxes with heavy fines and prison sentences.[314] Immediate passage of the tax reform plan is unlikely, however, since it is being bitterly opposed by the main opposition political party and by large segments of the private business sector.[315]

Given the current state of the tax system in Venezuela, it is the author's belief that a DL 157 device will not be forthcoming in Venezuela in the near future, nor is it certain that such a device would necessarily be successful. The conditions and problems in the Venezuela of today are quite different from those which induced and enabled Brazilian planner-technocrats to innovate in the mid-1960s.

It is the author's belief that the area in which there is room for greatest improvement is the protection of minority shareholder rights. Although the Venezuelan Capital Markets Law has provided some protective devices for shareholders, those that currently exist are not adequate and should be increased.

First, there is definitely a need for allowing direct shareholder inspection of company books and records. Even under the Capital Markets Law the shareholder still does not have this right; rather, this right of inspection is vested in the CNV. Suggested course of action is to allow for shareholder inspection of company books and records upon a reasonable request or showing of proper purpose. Additionally, it could be required that the person requesting inspection prove that he is a shareholder of record of at least 5 percent or else some similar appropriately established percentage.

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[311] Grant, *A Race Against Time*, Daily Journal [Ven], Feb. 28, 1977, at 2, col. 3.

[312] *Venezuelan Businessmen Speak Out Strongly Against Proposed Tax Reform*, BUSINESS LATIN AMERICA, Jan. 5, 1977, at 6-7.

[313] *Venezuela: Tough Talk*, LATIN AMERICAN POLITICAL REPORT, March 18, 1977, at 85-86.

[314] *Venezuelan Businessmen Speak Out Strongly Against Proposed Tax Reform*, BUSINESS LATIN AMERICA, Jan. 5, 1977, at 6-7.

[315] *Venezuela: Tough Talk*, LATIN AMERICAN POLITICAL REPORT, March 18, 1977, at 85-86.

Second, there exists a serious deficiency in the Capital Market's registration requirements in regard to the prospectus. As the law stands now, there is no requirement that the prospectus be received by the investor prior to making an investment decision. The extent of the law now is that an investor would either have to go down to the CNV to obtain the information on file, or else read it after it has been published in the National Securities Register. Provision should be made whereby the investor is readily able to obtain the prospectus well in advance of making an investment decision.

Third, there should definitely be provision in the Capital Markets Law expressly allowing private causes of action to be brought by injured shareholders. These provisions should specifically apply in the case of false registration information being filed with the CNV.

Fourth, there should be a provision allowing the CNV to effectively deal with securities violations involving misrepresentations, nondisclosure, and omissions of material facts (i.e., Section 10(b) and Rule 10b-5 type violations). In conjunction with this, there should be an express provision allowing injured shareholders the right to bring a private cause of action.

Fifth, provision should be made whereby "insider" trading by any corporate officials or employees is specifically prohibited. As part of this, any "short-swing" profits should be required to be paid back to the corporation. Both of these provisions should be vigorously enforced by the CNV.

Sixth, specific provisions should be made allowing both derivative suits and class actions to be brought by injured shareholders. Security fees or court costs should be kept to a minimum in these cases so as not to discourage shareholder suits.

Seventh, there should be stringent regulation of proxies and proxy solicitation. As it stands now, the Capital Markets Law does not even address proxy requirements or regulations.

Eighth, there should be a prohibition against over-the-counter securities trading. It should be required that all securities transactions be conducted on a regulated and authorized exchange.

Until these problem areas are adequately dealt with by the Venezuelan government, there is little reason to believe that public investor confidence in the market will increase appreciably. The law as it exists now does not offer adequate public investor protection.