SQUEEZE OUTS: THE ELIMINATION OF THE MINORITY PROBLEM
AND THE BASHFUL EVOLUTION OF CORPORATE LAW IN COLOMBIA.

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BOGOTÁ D.C.,
2015
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En cumplimiento de los requisitos para optar al título de abogado

Bogotá D.C., Agosto de 2015
ABSTRACT

Colombian corporate laws are protective of minority shareholders, and thus, are strictly prohibitive of squeeze outs, with the only exception of the Simplified Stock Corporation, which gives wide freedoms to majority shareholders.

Because neither case is truly effective, we propose an intermediate regulation that would allow duly justified squeeze outs that balance both the interest of the company and the rights of minority shareholders. We believe that such regulation may be facilitated by judicial review, as long as such judicial review is made on the basis of business standards and by duly qualified judges.

**Key Words:** Squeeze outs; minority shareholders; regulation.
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Artículo 23 de la Resolución N° 13 de Julio de 1946
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INTRODUCTION

This essay is aimed at assessing the following questions:

(i) How do squeeze out rights work?
(ii) What are the advantages of a squeeze out regulation?
(iii) Would such regulations be convenient in Colombia?

To that effect, this essay will analyze the role of the squeeze out in foreign systems, particularly the United States of America, will assess the pros and cons of such regulations, will review its partial adoption in the simplified stock corporation (Sociedad por acciones simplificada –S.A.S) statute—a significant yet insufficient step in the evolution of Colombian corporate law, and will generally set a preliminary framework of analysis to evaluate if it would be convenient, from a policy perspective, to introduce broad squeeze out regulations in Colombia.

In parallel, this paper will also provide a space of reflection on how Colombian corporate law has timidly started to move away from its classic trends –however mostly on the S.A.S., perhaps as a display of fear from change –, and has started to adopt institutions and instruments from the common law, particularly the United States, as a result of the corporate reality and practices in the country.

Squeeze outs are double-edged mechanisms which, when used in furtherance of an appropriate business or corporate purpose, can prove beneficial to corporate dynamics and increase the competitiveness of a business and even contribute to the evolution of corporate practices and law (mainly because it forces the minority shareholders to create protections against the squeeze –out). Still, the line between a beneficial squeeze out and the abuse of majority rights is often blurry.
Many legal systems worldwide have adopted squeeze out regulations, often focused on guaranteeing a fair compensation for the squeezed shareholders. In Colombia, except for simplified stock corporations and in that case only the case of mergers, spin offs, and “short-form mergers” (fusion abreviada), squeeze outs are not regulated and not generally allowed by statute. This would seem to evidence that the Colombian legislator fails to recognize that there are certain situations in which either the company or the shareholders might be better-off by excluding a shareholder who is causing disturbances, eliminate risks or costs associated with minority shareholders (mainly due to free-riders), or simply excluding a shareholder whose partnership is not desired by the rest of the company’s shareholders.

In the case of Colombia, the general rule for most forms of companies is a general prohibition of squeeze outs, and the provision of appraisal or sell-out rights for the minority shareholders, in an overly protective attempt to prevent cases of abuse of right perpetrated by the majority shareholders. This general rules has a notorious exception in the case of the simplified stock corporation, where squeeze out mechanisms such as short form mergers and cash out mergers are regulated (though with a limited scope). Nonetheless there does not seem to be any restriction as to squeeze out clauses or proceedings established in the bylaws, nor does the law seem to be concerned with compensation fairness in the context of cash out mergers; situation that could lead to further abuses of majority.

We believe that it is not prohibition but reasonable regulation that could give the squeeze out problem an efficient solution, and could lower the amount of cases of abusive or aggressive strategies performed by majority shareholders in trying to achieve complete control over a firm. Squeeze outs tend to respond to efficient business motives that cannot be disregarded, but the way to achieve those shall be regulated in such a way that does not imply “steamrolling” minority rights or affecting the necessary stability for minority investments.
1. **SQUEEZE OUTS AND THE RIGHTS OF MINORITY**

A squeeze out is often defined and understood as a mechanism used by controlling or majority shareholders to forcibly exclude the minority in exchange for compensation. Professor Vikramaditya Khanna and Umakanth Varottil from the University of Michigan and the National University of Singapore, respectively, define squeeze outs as follows:

“Squeeze outs are situations where the controller undertakes a transaction by which it forcibly acquires the remaining shares in the company held by the minorities through one or more available methods.”

And then add:

“Squeeze outs are both visible and palpable manifestations of a controller’s raw power within the corporate machinery—the ability to openly force minorities to accept a certain price for their shares.”

Then, squeeze outs are necessarily a transaction or business operation between an acquiring party and a forced selling party, aimed at making a firm “go private”. Professor Hyeok-Joon Rho’s, from the National University of Seoul, definition goes on a similar path, but is more specific on the transactional fashion of the squeeze out mechanisms:

“Generally speaking, a squeeze out is a mechanism used by a majority shareholders

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1 Although the expression “squeeze out” is used for this type of transaction in the Commonwealth as well other countries around the world, the expression “freeze-out” is more popular in the United States.


in a corporation to force out those in the minority. A squeeze out may be executed through various strategies including a cash-out merger, reverse stock split, two-step merger, or compulsory acquisition.

Squeeze out transactions may or may not imply a reduction of capital of the company, and may or may not involve a second company for its performance. The simplest option seems to be a scenario in which the controller acquires the shares of the minority (i.e. a Tender Offer) and cashes them out. A second scenario implies a re-acquisition of shares or a reimbursement of the capital contributions of minority shareholders. More complex transactions need the involvement of a second firm and are made in the context of a merger or an acquisition, but sometimes offer tax neutrality.

1.1. Squeeze Out regulation concerns.

A general concern when referring to squeeze outs is minority rights, as controlling shareholders usually have enough power to decide on the squeeze out and its conditions without regard to minority shareholders who may see their rights affected by the overpowering majority. Regulation can be very strict or costly depending on the approach it takes on this issue. As we will see ahead, protective measures are almost always directed towards avoiding abuse of majority, especially in what is related to price or consideration. What will also be made evident is that Colombian regulations do not seem to entirely follow this pattern.

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6 See id. at 502
7 See id. § 12.2, at 516.
8 See id. § 12.1, at 503.
Squeeze outs offer certain benefits, as they are often motivated by important business strategies that include, among others, (i) the integration of multiple business units of the controlling shareholder, (ii) cost efficient transactions, (iii) reduction of the company’s costs, (iv) reductions of risks related to abuse of minority, (v) elimination of free-rider shareholders, among others. These might represent big economic efficiencies that cannot be disregarded, even when considering the risks associated with squeeze outs.

Squeeze out regulations are often seen by academics and doctrine as a way to reduce cases of abuse, and even provide spaces for firm efficiency. In the words of Professor Hyeok-Joon Rho:

“In spite for concerns for minority shareholders, it is reasonable to seek legislation to minimize the negative aspects of squeeze outs rather than to simply deny the mechanism altogether. To reduce the risk of the majority’s exploiting the minority shareholders through squeeze outs, any squeeze out legislation should be carefully designed, thereby guaranteeing fair compensation for minority shareholders”

But at the same time, there are multiple debates and discussions as to the implications of squeeze outs in relation to the threat they pose to private property, the broad spectrum for opportunistic behavior that they permit and the violation of fiduciary duties.

Firstly, very broad squeeze out rights may lead to a general distrust of minority investors on a regime that would allow constant infringements to their right of peaceful enjoyment of private property. This scenario may be accompanied by a very small market for minority investments, which would be accompanied by a fall on prices for this type of investment as a consequence of

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12 Ibidem.
the high risks of being squeezed out and the higher transactional costs for this kind of investors.

Needless to say, a broad regulation leaves room for opportunistic and abusive behavior on the part of majority shareholders as a consequence of information asymmetries\textsuperscript{13}, and even situations of conflict of interests.

In fact, while minority shareholders are usually subject to the decisions taken by majorities as they do not have any control over the company, their investment incentives include the possibility of selling their participation (their shares market price), and their right to receive dividends. As a way to keep incentives for minority investments, local regulations often give some sort of veto right to minority shareholders in major decisions. Other protections include sell-out (or retirement) rights, by which the minority shareholder may sell its participation to the controlling shareholders forcing the purchase of their shares\textsuperscript{14}. These are especially applicable if the actions of the controlling shareholders have reduced the market for the company’s shares, or if the company’s business are no longer of the interest of the minority.

A regulation that allows squeeze outs without paying attention to minority’s motivations or interests will demotivate certain types of investments while openly allowing abuse situations. But more importantly, a regulation that is very strict on squeeze outs or creates high transactional costs may have a similar effect by creating perverse incentives on majorities to squeeze out minorities in seemingly legal ways, but based on abuse of their “raw power” over minorities.

Nonetheless, the most effective mechanism in favor of minority shareholders in the context

\textsuperscript{13} Because controlling shareholders generally have more information than the minority shareholders, they are prone to using that “privileged information” to determine squeeze out terms that are more favorable to them. Then, as a consequence of such information asymmetry and in a regime that establishes squeeze out compensation on a pre-freeze-out basis, minority shares are compensated at a lower value. (Kahan, Marcel y Lucian Arye Bebchuk. The Lemon Effect on Corporate Freeze Outs. National Bureau of Economic. Research Working Paper Series. Working Paper 6938. (1999): http://www.law.harvard.edu/faculty/bebchuk/pdfs/nber6938.00.kahan-bebchuk.pdf.)

of squeeze outs tends to be ex post remedies directed not towards the annulment of the transaction, but towards obtaining a fair compensation or claiming damages.

1.2. Squeeze Out Methods.

The first method that one can think of to perform a squeeze out, though it can be very costly, is achieved through the delisting of public companies. In most jurisdictions, a voluntary delisting process implies a delisting offer by which a controlling shareholder may be able to purchase the remaining shareholders equity participations\(^{15}\). This, however, hardly implies a forceful exclusion of minorities, but relies more on the will of the minority shareholders to sell. Also the price is to be determined by the methods determined by each Stock Exchange regulation, which may also carry high transactional costs.

A very common squeeze out mechanism in comparative law – in the context of Stock Exchange – lies in the possibility of a controlling shareholder or group of shareholders who have acquired a certain participation in a public company\(^{16}\) to force the remaining shareholders to sell their stockholding in the company so as to acquire 100% of the equity participation, therefore making the company “go private”. This is the case of the Short-Form Merger accepted in the


\(^{16}\) This participation often represents a majority so big that a risk of the company’s decisions not following the company’s interest but the controller’s interest is too big.
Model Business Corporation Act of the American Bar Association (which by 2012 had been followed by 31 of the 50 U.S. States\textsuperscript{17}), and similar cases are regulated in Germany\textsuperscript{18}, the European Union\textsuperscript{19}, and Argentina. The Argentinian case also involves a sell-out right for the minority along with the squeeze out right of the majority\textsuperscript{20}; a practice that, although successful, has been widely criticized for its similarity to a private expropriation, and its almost abusive nature.\textsuperscript{21}

A recent example of a two-step merger squeeze out is the recent acquisition of Jazztel by Orange in Spain. At the beginning of 2015, Orange launched a takeover bid over Jazztel for a price of $13 Euro per share. On 18 August 2015, in use of its squeeze out rights, Orange acquired the remaining 5% of the company and took it out of the Stock Exchange\textsuperscript{22}.

Another method is known as a “reverse stock split”. In a traditional stock split, the existing shares of a company are divided in multiple shares of less value (i.e. 2 for 1). A reverse split, as defined by the Securities Exchange Commission –SEC, is an operation by which a company “reduces the number of shares and increases the share price proportionately”\textsuperscript{23}. Using this...


\textsuperscript{21} Ibídem. Page 300.

\textsuperscript{22} "Jazztel abandona la Bolsa tras controlar Orange el 100% de la empresa.” El Confidencial 18 August 2015: \texttt{http://www.elconfidencial.com/empresas/2015-08-13/jazztel-abandona-la-bolsa-tras-controlar-orange-el-100-de-la-empresa_967683/}; "Orange completa la compra del 100% de Jazztel, que dejará de cotizar mañana." eleconomista.es 18 August 2015: \texttt{http://www.eleconomista.es/tecnologia/noticias/6944081/08/15/Orange-completa-la-compra-del-100-de-Jazztel-que-dejara-de-cotizar-manana.html}; and "Jazztel abandona la Bolsa quince años después de su debut tras su compra por Orange. El Mundo 13 August 2015: \texttt{http://www.elmundo.es/economia/2015/08/13/55cb4b2246163f45698b4582.html}.

method, which at least in the United States does not need the shareholders meeting approval\textsuperscript{24}; shareholders who have a smaller amount of shares can be cashed out – depending on the ratio used – at lesser expense than with other transactions. The remaining shareholders may, later, perform a forward stock split to undo the stock merge.

Methods outside the stock exchange (though they can sometimes involve publicly traded companies) involve mergers. The simplest example of this is a merger among company A, wholly owned by X, and company B, where X is a controlling shareholder. As a consequence of the merger, company A absorbs company B, and, in exchange for their shares, shareholders from company A receive consideration in cash or in shares of a third company. As a result, these shareholders are effectively squeezed out. The effective combination of a tender offer and a merger is often referred to as a two-step merger.

Another good example, if successful, could be the acquisition of Alcatel-Lucent by Nokia Corp. Last April, Nokia and Alcatel CEO’s agreed on the terms of a transaction by which Nokia would acquire Alcatel through a tender offer, and compensate Alcatel’s shareholders with shares of Nokia.\textsuperscript{25}

\section{Squeeze Outs in Other Jurisdictions}

\subsection{Canada}

Fundamental changes – acts or transactions that imply transformations or relevant changes of a company – are regulated on part XV of the Canadian Business Corporations Act (from now on, the \textbf{CBCA}). The two following parts of the CBCA dictate general rules for going-private

\begin{flushleft}
\textsuperscript{24} Ibídem.
\end{flushleft}
transactions and squeeze out transactions, and regulate compulsory and compelled acquisitions, mostly referring to takeover bids.

Pursuant to Section 193 of the CBCA any corporation may perform a “going private” transaction if the applicable provincial securities law allows such transaction. Furthermore, article 194 of the CBCA reads:

“A corporation may not carry out a squeeze out transaction unless, in addition to any approval by holders of shares required by or under this Act or the articles of the corporation, the transaction is approved by ordinary resolution of the holders of each class of shares that are affected by the transaction, voting separately, whether or not the shares otherwise carry the right to vote. However, the following do not have the right to vote on the resolution:

a. affiliates of the corporation; and

b. holders of shares that would, following the squeeze out transaction, be entitled to consideration of greater value or to superior rights or privileges than those available to other holders of shares of the same class.”

Then, under general Canadian corporate law, any squeeze–out transaction is subject to approval by an ordinary meeting of the shareholders of each class of shares in the company, separately\(^\text{26}\). This, as in the Indian case (as will be explained below), might find foundations in the belief that because different kinds of shares carry different rights, then their interests are dissimilar and thus, must be addressed separately. However, interestingly enough, Canadian law’s also differentiate among holders of the same class, when it provides that holders of shares that would be entitled to the higher consideration after being squeezed out than the remaining

\(^\text{26}\) As will be shown above, this is also a requisite for some squeeze out transactions in India.
shareholders from the same class, are not entitled to vote on the resolution that approves the transaction.

Furthermore, Canadian Squeeze Out transactions are subject to an oppression remedy, which evaluates the transaction in equity or fairness, which forces squeeze out transactions to be based upon:

“The oppression remedy focuses on harm to the legal and equitable interests of a wide range of stakeholders affected by oppressive acts of a corporation or its directors. This remedy gives a court a broad jurisdiction to enforce not just what is legal but what is fair. Oppression is also fact specific: what is just and equitable is judged by the reasonable expectations of the stakeholders in the context and in regard to the relationships at play. [45] [58-59]

In assessing a claim of oppression, a court must answer two questions: (1) Does the evidence support the reasonable expectation asserted by the claimant? and (2) Does the evidence establish that the reasonable expectation was violated by conduct falling within the terms “oppression”, “unfair prejudice” or “unfair disregard” of a relevant interest?”27

Canadian Law offers multiple squeeze out possibilities, and regulation is most of the times directed towards achieving a balance between business purposes and minority shareholders’ interests.

a. Plan of Arrangement

In Canada, acquisitions are most commonly performed under a “statutory plan of

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27 BCE Inc v 1976 Debentureholders, 2008 SCC 69 (CanLII), [2008] 3 SCR 560
arrangement”\textsuperscript{28}.

Under a plan of arrangement, a squeeze out should be approved not only by shareholders in the terms of section 193 of the CBCA, but is also subject to court approval in the terms of article 192(3)\textsuperscript{29}. In general terms, an agreement would be approved by the court whenever it has a valid business purpose, and the interests and objections of opposing shareholders are addressed and resolved in a “fair and balanced way”\textsuperscript{30}.

In a very different approach to that taken by the courts of Delaware, in establishing the fairness of a plan of arrangement the court focuses on other factors other than the process of the arrangement:

“In determining whether a plan of arrangement should be approved, the court must focus on the terms and impact of the arrangement itself, rather than on the process by which it was reached. What is required is that the arrangement itself viewed substantively and objectively, be suitable for approval.

In seeking approval of an arrangement, the corporation bears the onus of satisfying the court that: (1) the statutory procedures have been met; (2) the application has been put forward in good faith; and (3) the arrangement is fair and reasonable (...) On these appeals, it is conceded that the corporation satisfied the first two requirements. The only question is whether the arrangement is fair and reasonable.”\textsuperscript{31}

As explained by Matthew Cumming, partner in the Business Law Group of MacCarthy

\textsuperscript{28} IBA Corporate and M&A Commitee. Canada - Squeeze Out Guide. 2010. Page 1
\textsuperscript{29} “Where it is not practicable for a corporation that is not insolvent to effect a fundamental change in the nature of an arrangement under any other provision of this Act, the corporation may apply to a court for an order approving an arrangement proposed by the corporation.”
\textsuperscript{31} Ibidem. Paragraph 136
Perrault firm in Toronto:

“A plan of arrangement enables the bidder to be creative in structuring the transaction in order to realize any commercial and tax objectives of the deal. Courts are capable of dealing with complex acquisition structures and have affirmed that a central purpose of the arrangement provisions in the corporate statute is to enable this.”\(^3\)

The IBA guide to squeeze outs in Canada explains the plan of arrangement as follows: “Under a plan of arrangement, the acquisition is required to be approved by a court and by the target company’s shareholders. Subject to those approvals being obtained and any other closing conditions being satisfied, every share of the target company is exchanged at closing for the consideration offered under the plan, which is typically cash or securities of the purchaser, or a combination of the two. As a result, where an acquisition is completed by way of a plan of arrangement (or another shareholder-approved transaction, such as a statutory amalgamation), the purchaser is able to acquire all of the outstanding shares of the target company in one step, with the result that no minority shareholders remain, and a subsequent squeeze out transaction is not required.”\(^3\)

Plans of arrangement are usually friendly transactions that are very flexible in structure. Furthermore, because a plan of arrangement is subject to court approval, shareholders opposition is not a determinant factor to the success of the transaction.

\(b.\) \textit{Takeover Bids}

\(i.\) \textit{Compulsory acquisition}

\(^3\) Ibid. Page 1
An amalgamation squeeze out is very similar to a merger squeeze out, nonetheless, unlike a merger, an amalgamation often implies that the amalgamated entities are absorbed into a third new entity.

“In an amalgamation squeeze, the target corporation is amalgamated with a second corporation controlled by the majority shareholder. The terms of the amalgamation provide that the minority shareholders, upon completion of the amalgamation, will not receive participating securities in the amalgamated corporation but instead will be given either cash or, more typically, redeemable preferred shares that will be promptly redeemed for cash.”

The CBCA subjects this amalgamation to approval by a 2/3 majority in the shareholders meeting of the amalgamated corporations, which might make the transaction easier if the controlling shareholder owns 67% or more of the company’s shares. Nonetheless, it is important to note that a two-step transaction will require that the transaction followed by a bid to be approved not only by 2/3 of the shareholder meeting, but also by a majority of the minority.

ii. Amalgamation Squeeze out

An amalgamation squeeze out is very similar to a merger squeeze out, nonetheless, unlike a merger, an amalgamation often implies that the amalgamated entities are absorbed into a third new entity.

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c. **Share Consolidation**

A share consolidation or reverse stock-split is performed through an amendment to the bylaws. The CBCA provides that such decision shall be approved by a special resolution of the shareholders meeting, which requires a 2/3 majority.

To effectively squeeze out the minority shareholders through a share consolidation, the amendment has to establish a cash out provision for fractional shares, and the exchange ratio has to be such that minority shareholders would be left with fractional shares that, even if amounted together, could not add a full share.

d. **Conclusions**

Canadian law provides for squeeze out mechanisms that either require a shareholder authorization with a special majority, or that are subject to ex ante court sanction. Moreover, if made through a method other than a plan of arrangement, unhappy squeezed out shareholders can

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37 Ibid. Page 414.
still take the transaction to court to demand reparation or fair value over their shares.

The option of a plan of arrangement is one of the most interesting alternatives. Though it can represent high transactional costs, the court approval in a way “ironclads” the transaction while ensuring that both the controllers and the minority shareholders interest are protected and addressed; furthermore, it offers a wide range of transactional structure possibilities.

Finally, it is worth mentioning that (at least in the case of the plan of arrangement), this type of regulation can only be effective if there are specialized judges that can correctly address any of the issues that might come up, and that are capable of understanding complex transaction structures.

A notable example of a Canadian plan of arrangement is the acquisition by Pacific Rubiales of Petrominerales. In this transaction, both companies executed a plan of arrangement by which Pacific Rubiales would acquire every share of Petrominerales in exchange of cash and a shares in Alvopetro Energy Ltd., a newly established company which now hold all the Petrominerales assets in Brazil.39

2.2. South Korea

In a similar fashion to the Colombian context, “(...) many Korean companies have dominant or controlling shareholders, and the level of general protection for minority shareholders is still limited in Korea”40, thus, squeeze out regulation might be a sensitive, yet very important matter for corporate regulation.

On the other hand, Korean minority shareholders seem to have become more active in

recent years, and with the aid of new regulation like the Securities Class Action Act of 2005\textsuperscript{41} they may have more tools towards becoming more active before company administrators.\textsuperscript{42} More active minority shareholders tend to imply that the administration costs associated with minority may increase, and as a matter of fact, Professor Hyeok-Joon Rho has associated the growing shareholder activism tendencies with a phenomenon of increasing demands for delisting\textsuperscript{43}. Such request for delisting is usually preceded by a tender offer by the controlling shareholders as a way to offer an exit opportunity to the minority shareholders.

"Under the KCC [Korean Commercial Code] a majority shareholder may try to squeeze out minority shareholders through such oppressive methods as limiting dividends, changing the corporate structure, of siphoning off earnings\textsuperscript{44}, some of which are also used to some extent in the Colombian context for forcing minority shareholders to sell off their equity participations to a controlling shareholders, but are considered to be abusive and thus can be punished by the Colombian Superintendence of Companies. The context in which such oppressive and abusive methods can be used is also limited in Korea, as Sections 368, 538, and 464 of the Korean Commercial Code provide protections to minority shareholders in relation to dividends and voting rights.\textsuperscript{45}

The following are the methods provided by Korean Law for the performance of squeeze out transactions:

\ \ \ \textit{a. Cash Out mergers}

Even if the Korean Commercial Code does not expressly mention cash out mergers, and

\begin{itemize}
  \item Ibid. Page 65.
  \item Ibid. Page 66.
  \item Ibid. Page 66.
\end{itemize}
by general rule it is expected for shareholders of the absorbed company in a merger to receive shares on the absorbing company or the resulting entity, Section 523.4 of the KCC allows the acquirer to agree on paying cash to the shareholders of the acquired company, and establish the terms of such consideration on the merger agreement.

This method, however, cannot be used in short-form or abbreviated mergers where a company merges its 90% owned subsidiary.\(^\text{46}\)

\(b. \) \textit{Share Transfer and Share Exchange}

Article 360.2 of the KCC regulates the “Share Exchange”, a transaction by which all the shares of the target company can be transferred to the acquiring company, giving the buyer the complete ownership over the target. Nonetheless, shareholders from the target company are expected to receive shares in the acquiring company.

In the case of the “Comprehensive Share Transfer” of article 360.15 of the KCC, a new entity is incorporated, and the shareholders from the target company then receive shares in such new entity (which becomes a holding company to the target).

Both the aforementioned mechanisms are compulsory, even for dissenting shareholders, if the transaction is approved by the shareholders meeting of both the target and the acquiring company. Even if it is not a proper squeeze out mechanism, in Korea, it was seen as step towards squeeze out regulations for its forceful nature.\(^\text{47}\)

\(c. \) \textit{Conclusions}

The obstacles imposed by Korean regulation on squeeze outs makes it very difficult for majority shareholders to squeeze out minority shareholders, thus making it a common practice to recur to more violent methods which tend to demotivate the minority’s investment forcing them

\(^{46}\) Section 527.2 of the KCC. Ibidem. Page 67.
to sell out.

This very strict regulation, then, proves to be very ineffective in both protecting minority rights while allowing majority interests towards efficiency.

2.3. **India**

In India, yet again like in Colombia and Korea, most companies have controlling shareholders, which creates a corporate scenario that seems to be very prone to squeeze outs\(^48\). Indian corporate regulation, particularly India’s Companies Act of 2013 which replaced the Companies Act of 1956, provides for most of the squeeze out methods, and minority protection mechanisms, that we will overview now.

a. **Delisting**

The Securities Exchange Board of India (“SEBI”) Delisting of Equity Shares regulations of 2009 (from now on the “SEBI Delisting Regulations”), to be updated by an amendment announced earlier this year, “enable a company to delist its equity shares on the stock exchange so long as the public (or the non-controlling shareholders) are given an exit opportunity”\(^49\).

In a similar fashion to the regulation on the Colombian Stock Exchange, the Indian delisting implies a compulsory offer to acquire shares (made by the controlling shareholder). SEBI Delisting Regulations provide for the compulsory use of the reverse book building\(^50\) method to set the price on the shares. The controlling shareholder then can either accept or refuse the offers; if it accepts the offer, the controller shareholder then shall acquire the shares at the final tendered price.

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\(^{49}\) Ibid. Page 10.  
\(^{50}\) Under the reverse book building pricing method, a floor price is determined based on the historic value of the share, and their trading value. Shareholders then make offers over their shares, which shall be above or equal to the floor price.  
http://www.nseindia.com/products/content/equities/ipo/Reverse_bookbuilding.htm
The delisting decision is to be approved by the shareholders general meeting with a 75% majority, with the additional requisite of at least 2/3 of the minority shareholders casting a favorable vote. This veto right takes away the controlling shareholders position to annihilate or “steamroll” the minority, by forcing them to thrive for the minority’s cooperation, therefore enervating the controller’s possibility to abuse its advantages.

According to authors Vikramaditya S. Khanna and Umakanth Varotttil, this method is “too onerous for controllers” and therefore it is not usually used, and if used, it tends to not be very successful due to excessively expensive final offer prices.\(^5\)

\(b. \quad \textit{Scheme of arrangement}\)

One of the most interesting possibilities for squeeze outs in Indian Law might be the one known as Scheme of Arrangement. As provided in Section 230 of India’s Companies Act, companies can enter into arrangements with their shareholders and their creditors; it is through such arrangements that a company may be part of a strategy by which the company itself, or its controlling shareholder, can acquire the minority shares and squeeze them out.

“The process begins with the company applying to the High Court to convene meetings of the various shareholder classes. The scheme must be approved by a majority in number representing 75\% in value of each class of shareholders present and voting, in separate meeting for each class\(^5\). Once approval is obtained, the company must again approach the High Court for sanction of the scheme.”\(^5\)

This method, however, involves high costs and heavy court involvement, which may

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52 This represents a dual majority requirement. The scheme must be first approved by a majority of shareholders in number from among those who are present and voting. At the same time, those voting in favor of the scheme must also hold 75\% in value of the aggregate shares (held by those who are present and voting).
reduce its benefits to: (i) the High Court’s involvement is a strong protection for minority shareholders, and (ii) if the arrangement provides for the company to re-acquire the shares, the controlling shareholder does not have to assume any of the costs.

c. **Compulsory acquisition**

Section 235 of India’s Companies act of 2013 allows companies to perform compulsory acquisitions only if regulated in the company’s bylaws. In compliance with the aforementioned provision, the majority shareholder shall make a takeover offer to the remaining shareholders. If at least 90% of the recipients accept the offer during the four months following the offer, the offeror shall serve notice to the remaining shareholders to perform a compulsory acquisition on their shares on the same terms as the initial offer. The aforementioned offer can be made in cash, or in shares from another company, and any dissenting shareholder has the possibility of coming before India’s National Company Law Tribunal to demand remedies, but only before the transaction has been performed.

The requirements to perform a compulsory acquisition make it very rare in practice. A shareholder with a high equity participation that does not reach 90% may need to make multiple offers to achieve such 90% threshold, and then proceed to make a takeover bid, just to squeeze out the remaining shareholders; which may create high transactional costs. Moreover, the situation gets even more complicated if shares held by beneficial owners are not counted for the 90% requirement.\(^{54}\)

d. **Reduction of capital**

Section 66 of the Indian Companies Act allows a company to reduce its capital by repurchasing and cancelling a number of its circulating shares if the conditions of Section 100(1) are met.\(^{54}\)

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of the same statute are met.

The reduction of capital shall me approved by 75% of the votes cast, through a special resolution of the shareholders meeting. Then, the company must apply before the High Court and request the sanction of such resolution. The ruling shall then be registered.

This method, as well as the last one, provides a good degree of minority protection, while the costs of the transaction affect the company and not the controlling shareholder (not directly).

e. Conclusions

As seen, India seems to have a comprehensive and seemingly efficient squeeze out regulation, that offers guarantees to minority shareholders and, while posing certain obstacles in the controlling shareholder’s way, it allows for majority to take full control over companies.

Nonetheless, Indian regulation is still very strict, making it very difficult to squeeze out shareholders in situations that might bring further efficiencies, such as the case of free-rider shareholders or activist shareholders.

2.4. Delaware

The United States corporate scene is characterized by companies with a very dispersed shareholding structure in which it is very rare to find a company in which a single shareholder (or beneficial owner) has enough power to take decisions. Also, the United States corporate law and Stock Exchanges are often recognized as sophisticated institutions, and many of their advances are often replicated elsewhere. In Colombia, Law 1258, as we will see later on, has replicated –to some extent –some institutions from U.S law, such as the short-form merger.

The corporate context in the United States tends to be much more active and dynamic due to the disperse ownership structure of the companies, and the board of directors tends to have a lot more power than in more static scenarios like the Colombian case. It is no surprise then, that
many of the most sophisticated and interesting corporate phenomena are born or developed in the United States. Examples of this, are practices as hostile takeovers, and consequently defense tools such as poison pills; and the ongoing and increasing phenomena of shareholder activism.

On this section 2.4 I will address Delaware corporate law in relation to freeze outs.

Even when many of the U.S. states have very interesting regulations (i.e. California or New York), Delaware has been an important center for corporate law development in the U.S. due to the vast concentration of companies incorporated or headquartered in the State\(^5\). This concentration of companies is often attributed to both tax and regulation flexibility, which makes Delaware an exception in many cases, but also a very interesting study subject.

In this section, I will review some of the relevant provisions of the Delaware General Corporation Law (from now on “DGCL”), and some of the most discussed case law pertaining to freeze outs.

It wasn’t until the 1920’s that the possibility of cashing out minority shareholders was allowed in the United States, with Florida being the first state to allow cash-out mergers. The state of Delaware authorized cash consideration in short form mergers in the early 1950’s, and 10 years later on long-form mergers\(^6\). By the end of the 1960’s the Model Business Corporation Act\(^7\) also incorporated cash out rules for both long form and short form mergers. Some years later, however, States, and the United States Securities and Exchange Commission –SEC, were

\(^5\) According to the official web page of the State of Delaware, “The State of Delaware is a leading domicile for U.S. and international corporations. More than 1,000,000 business entities have made Delaware their legal home. More than 50% of all publicly-traded companies in the United States including 64% of the Fortune 500 have chosen Delaware as their legal home.”, then adding that “The Delaware General Corporation Law is the most advanced and flexible business formation statute in the nation.” [http://www.corp.delaware.gov/aboutagency.shtml](http://www.corp.delaware.gov/aboutagency.shtml)


\(^7\) The Model Business Corporation Act, often referred to as MBCA, is a model of corporation law prepared and updated by the American Bar Association as a way to unify corporate law in the united states and thus clarify certain issues. The MBCA is followed at some degree by most of the States in the U.S.
trying to incorporate protections to minority shareholders without banning freeze outs\textsuperscript{58}, thus one of the major issues on U.S law when it comes to squeeze outs is fairness, both on the price and on the dealing\textsuperscript{59}.

Delaware law allows most –if not all –of the abovementioned freeze out methods, nonetheless, the most studied (and perhaps the most used), seem to be tender offers and mergers.

\textit{a. Cash Out Mergers}

Section 251 of the DGCL allows for two or more companies to merge into one (either forming a newly incorporated entity, or through an existing corporation absorbing the remaining merging entities). Paragraph (b) of Section 251 provides that the board of directors of the merging entities shall approve a resolution approving the merger agreement which shall contain, among others, the manner in which the share of each merging entity are to be converted, or the stipulation by which certain shares are to be cancelled and paid in “the cash, property, rights or securities of any other corporation or entity which the holders of such shares are to receive in exchange for”. The terms of trade may include a mix of various methods of compensations.

Such decision shall be taken to the shareholders annual or special meeting, for which the summoning shall contain the merger agreement on the meeting’s agenda, and the agreement shall be submitted to every shareholder at least 20 days prior to the meeting.

By rule, such transaction can be approved by a simple majority, though, as we will analyze later, if done with the approval of the majority of the minority, judicial review standards might shift.

\textit{b. Tender Offers and Two-Step Mergers}

\textsuperscript{59} This was explained by the Delaware Supreme Court in the ruling Weinberger v. UPO (457 A.2d 701, 711 (Del. 1983).
As seen earlier, squeeze outs can be performed through tender offers, where the controlling shareholder makes a purchase offer to the remaining shareholders. If the offer is accepted by all the minority shareholders, the controller will purchase their shares at the conditions of the offer, and acquire complete control over the company thus making it “go private”.

A two step merger often happens when the controlling shareholder is not able to acquire the shares of all the minority shareholders through a tender offer. If it acquires enough to own 90% or more of the company’s shares, then after the tender offer it will be in capacity of performing a short-form merger and force the exit of the remaining shareholders. If such supermajority is not achieved, the controller shall perform a regular cash-out merger to squeeze out the remaining minority shareholders.

As will be analyzed below, case law has created differentiated among types of transactions for applying different standards of judicial review. As per tender offers, the courts of Delaware have held that “(...) tender offers do not warrant entire fairness because, in this transaction, in contrast to a merger, minority shareholders are protected by the decision itself of tendering or not tendering”60. Later on, by applying business judgment to short-form mergers, some two-step mergers were also exempted by the Delaware Supreme Court from fairness review.

c. Supermajorities and Short Form Mergers

Section 253 of the DGCL establishes the rules of the “Merger of parent corporation and subsidiary or subsidiaries”, otherwise known as Short-Form Merger, which is performed under

rules similar to that of article 33 of the Colombian Law 1258.

The provision of the aforementioned section 253 establishes that when at least 90% of the outstanding shares of each class of the stock of a corporation or corporations is owned by another corporation, such parent company “may either merge the other corporation or corporations into itself and assume all of its or their obligations, or merge itself, or itself and 1 or more of such other corporations, into 1 of the other corporations”.

This merger is to be approved by the board of directors of both the parent and the subsidiary corporations. The resolution by which the board approves the merger shall include the terms in which minority shareholders of the merged subsidiaries shall be compensated, be it “securities, cash, property, or rights”.

d. The Entire Fairness Review, the Business Judgement and other Procedural Protections

As explained by Fernan Restrepo in “A re-examination of Silliconix”, entire fairness has been a traditional protection for minority shareholders, since the State of Delaware authorized squeeze out transactions:

“Entire Fairness Review has been a protection for minority shareholders in merger freeze outs since 1952, when the Delaware Supreme Court in Sterling v. Mayflower Hotel Corporation61 and Gottlieb v. Heyden Chemical Corporation,62 held that the minority in those transactions are entitled to a judicial reassessment of the price paid by the controller if they consider that price to be unfairly low.”63

Until 2001 squeezed out shareholders could request an “entire fairness” review, in which

61 93 A.2d 107, 109 (Del.1952)
62 91 A.2d. 57, 58 (Del. 1952)
a judge would analyze if the squeeze out transaction was performed fairly in both the dealing and the price. While fairness in the dealing refers to the timing of the transaction, its timeline, its structure and negotiation, as well as its disclosure to the directors and the shareholders, as well as how their approvals were obtained; fairness in the price\(^{64}\) has to do with the consideration paid to the shareholders and the economic and financial reasons behind it.\(^{65}\) Moreover, the entire fairness review, although having two main components, shall be analyzed in a non-bifurcated approach.\(^{66}\)

After 2002 the United States started experiencing an increase of squeeze out activity, particularly in public firms that started going private\(^{67}\). Around that time, Delaware case law started shifting, with the case “in re Silliconix Incorporated Shareholders Litigation” of the Delaware Chancery Court being one of the most relevant, and established different standard of judicial review of different types of freeze-out:

“Delaware case law created a difference in the standard of judicial review for the two basic methods of freezing out minority shareholders. While a freeze-out executed as a statutory merger is subject to stringent “entire fairness” review, the Delaware Chancery Court held in In re Siliconix Shareholders Litigation that a freeze-out executed as a tender offer is not.”\(^{68}\)

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\(^{64}\) As pointed out by Allen, William T., Kraakman Reinier and Guhan Subramanian, “Only the speculative elements of value that may arise from “accomplishment or expectation” of the merger are excluded, (...) But elements of future value, including the nature of the enterprise, which are known are susceptible of proof as of the date of the merger and not the product of speculation, may be considered”. Allen, William T., Kraakman Reinier y Guhan Subramanian. Comentaries and Cases on the Law of Business Organization. Second Edition. New York: Aspen Publishers, 2007. Page 506.


\(^{68}\) Ibid. Page 1.
A month later, the Delaware Supreme Court ruled in Glassman v. Unolocal Exploration Corporation that short form mergers were also excluded from the entire fairness review. Thus, after 2001, squeeze outs performed in Delaware under a tender offer, a short form merger, and some forms of two-step mergers are not subject to the entire fairness review.

This point was later reinforced by the Delaware Supreme Court in Glassman v. Unolocal Exploration Corporation, were the court held that the objectives and benefits of the simplified procedure for a merger under Section 253 of the DGCL would be lost if the “fiduciary duties owed to minority shareholders were interpreted as they were in the context of ordinary statutory mergers”.

Furthermore, as evidenced by both professor Subramanian and Fernan Restrepo, in the early 2000’s the Delaware Supreme Court started shaping a procedure to be followed on squeeze out transactions. The procedure, as explained by professor Subramanian, would be the following:

“The traditional route for executing a freeze-out uses the process outlined by the Delaware Supreme Court in Weinberger v. UOP and Kahn v. Lynch Communication Systems: the target board establishes a special committee (SC) of directors who are independent from the controller; the SC hires bankers and lawyers to advise it; and the SC negotiates with the controller over the terms of the deal, most importantly the price to be paid to the minority shareholders and whether the deal will include a non-waivable majority-of-the-minority (MOM) closing condition. If the controller and the SC reach agreement, the deal is submitted for the necessary board

69 Restrepo, Fernan., Page 323.
70 Ibid. Page 327.
71 457 A.2d 701, 709 n.7 (Del. 1983).
72 638 A.2d 1110 (Del. 1994).
and shareholder approvals. If approved, the transaction is typically executed as a statutory merger or a two-step tender offer (that is, a first-step tender offer followed by a short-form merger), though occasionally it is structured as a reverse stock split or an asset acquisition by the controlling shareholder.\footnote{Subramanian, Guhan. Op. Cit. Page 3.}

Firstly, in accordance to what the court upheld in Weinberger v. UOP, “\textit{target boards should form a special committee of independent directors to negotiate the terms of the deal with the controller and, in this way, increase the likelihood of satisfying the two prongs that make a transaction “entirely fair”}.\footnote{Restrepo, Fernan. Op.Cit. Page 325.} The inclusion of such special committee, as later explained by the court on Kahn v. Lynch Communication Systems, shifted the burden of proof on entire fairness (from the defendant to the plaintiff).\footnote{Restrepo, Fernan. Op.Cit.. Page 326; Allen, William T., Kraakman Reinier y Guhan Subramanian. Page 514.}

Later, on Rossenblatt v. Getty Oil Co.\footnote{493 A.2d. 929, 937 (Del. 1985)} the Supreme Court held that “\textit{merger freeze-outs approved by the MOM were also subject to the entire fairness review (although, again, the burden of proof shifts to the plaintiff if the minority shareholders approve the deal) (...)”}.\footnote{Restrepo, Fernan. Op.Cit. Page 326.}

Nonetheless, the conditions to determine whether a case is to be examined under entire fairness or business judgment are far less simple than shown above. As evidenced by Fernan Restrepo, short form mergers and tender offers could still be subject to entire fairness instead of business judgment\footnote{Business judgment, like in Colombia, implies that there is a presumption that company administrators perform their duties in good faith and in compliance with their fiduciary duties. Then, their decisions are not to be reviewed unless proved that the later were not complied with. \textit{See} Allen, William T., Kraakman Reinier y Guhan Subramanian. Op.Cit.} under certain conditions:

\textit{“(...) In re Pure Resources [In re Pure Resources Litigation], the Delaware Chancery}
Court held that business judgment only applies to offers that are not coercive, and that an offer is non-coercive if it meets three conditions:

(i) there is a non-waivable MOM condition; (ii) the controlling shareholders guarantees to consummate a prompt shot-form merger at the same price if he obtains 90% or more of the shares; and (iii) the controlling shareholder makes no retributive threats in its negotiations with the special committee.”

Finally, in 2013 Delaware’s Chancery Court held that deals approved by both the MOM and a special committee were not subject to entire fairness, but business judgment\textsuperscript{80}, in a way, applying the approach of Vice Chancellor Strine in In re Pure Resources Litigation, according to which business judgment should be applied to transactions performed at arm’s length, and the remaining should be subject to entire fairness\textsuperscript{81}.

The aforementioned was once again upheld by the Delaware Supreme Court on 2014, in the case Kahn v. M&F Worldwide Corporation\textsuperscript{82}, but this time, the court authorized the application of the business judgment to squeeze out mergers, if the transaction complied with the requirements established in the aforementioned cases\textsuperscript{83}. Nonetheless, Kahn v. M&F Worldwide Corporation required the defendants to demonstrate the following six requirements in order to prove that the standards were in fact complied with:

[We did not add the references]“To make sure that an independent, adequately-empowered Special Committee was operational and meeting its duty of care, and that

\begin{itemize}
\item \textsuperscript{80} Restrepo, Fernan. Op.Cit. Page 326. The author refers to In re MFW shareholders litigation and In re CNX Gas Corporation Shareholders litigation.
\item \textsuperscript{81} Ibid. Page 329.
\item \textsuperscript{82} 88 A.3d 635 (Del. 2014).
\end{itemize}
the shareholder vote was un-coerced and informed, the defendants must demonstrate that they have fulfilled the following six requirements: (i) the controller conditions the procession of the transaction on the approval of both a Special Committee and a majority of the minority stockholders; (ii) the Special Committee is independent; (iii) the Special Committee is empowered to freely select its own advisors and to say “no” definitively; (iv) the Special Committee meets its duty of care in negotiating a fair price; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority.”

The latter is justified on the belief that the aforementioned requirements deprive the controller to command the results of the transaction based on its prerogatives and powers derived from majority. By performing the transaction at arm’s length and giving minority shareholders the possibility of opposing the transaction or the proposed terms, fairness should be achieved without need of judicial control.

e. Conclusions

The State of Delaware has a flexible regulation that allows squeeze out transaction through somehow easy methods, some with more transaction costs than others, while protecting minority shareholders in their economic interests. Furthermore, regulation seems to also seek that the squeeze out is performed with due negotiations and appropriate proceedings.

Delaware courts, recognizing that sometimes squeeze out transactions may be hostile or aggressive towards the minority shareholders, seek to incentive negotiated transactions through distinctions in judicial review. The distinction between arm’s length and non-arm’s length transactions proves to be an efficient regulation, as controlling shareholders are encouraged to

carry the squeeze out according to procedures that protect minority; and when such proceedings are disregarded, the interests of the minority shareholders are protected by a thorough examination of fairness in both price and dealing. Then, minority shareholders are protected, but the global benefits of squeeze out transactions are not lost to either society or controllers.

However, it is important to consider the findings of both professor Subramanian in “Post-Siliconix Freeze-Outs”, and Fernan Restrepo in “A re-examination of Siliconix”, according to which, after the differential standard of review created by the Siliconix case law, shareholders squeezed out after a tender offer are more prone to receive lower returns than before the Siliconix differentiation, and lower returns than shareholders squeezed out through merger transactions, proving that regulation does in fact have an effect on shareholder compensation.85

3. SQUEEZE OUTS IN COLOMBIA

3.1. Current Corporate Panorama

Until 2008, Colombian corporate law incorporated only four main types of corporations, which were much regulated by the Colombian Commercial Code, thus leaving little space for the partners’ contractual freedom on the bylaws. Furthermore, certain rules drastically change among types, depending on the nature of the company as a “capital company” (sociedad de capital), or a “partnership” (sociedad de personas).

For instance, the rules of partnerships are set under the assumption that the company’s main component is the partners themselves. The law assumes that a set of people with certain values, ideas, or characters decides to start a company, and thus, the qualities and characters of any partner at any given time is of upmost relevance to the company itself. Under that set of

ideas, the partners themselves are in charge of the administration of the company, and are personally liable for the company. In fact, partners are so important in partnerships that the exit or entering of any partner necessarily implies an amendment to the bylaws, which is only possible by unanimous decision of the board of partners, through a public deed.

On the other hand, capital companies are established upon money or capital contributions. The qualities or values of the shareholders are not relevant, as much as the contributions made to the stockholder’s equity. In light of this, shares are more easily negotiable than quotas, and the shareholders’ participation on the company’s administration is generally reduced to participation in the shareholders assembly or the board of directors.

Likewise, establishing rules in the bylaws to exclude a partner in a partnership proves to be easier than in a capital company, and is thoroughly regulated by the Colombian Code of Commerce, though with some limitations, and generally accepted by the Colombian Superintendence of Companies. Contrariwise, the Superintendence of Companies has stated in multiple concepts that, even with the lack of express prohibition, the stipulation of squeeze out rules or shareholder exclusion rules is not possible on a Stock Corporation (Sociedad Anónima – S.A. which is considered to be the Colombian capital company by definition), as it is considered to be contrary to the spirit of such company type\(^{86}\), and thus an infringement of paragraph 14 of article 110 of the Code of Commerce.

In 2008, Colombian corporate law experienced a great leap forward with the enactment of Law 1258, which created the simplified stock company, finally giving business a more dynamic option, and addressing many of the market needs by giving more freedom to the shareholders in the bylaws, and incorporating many of the advances of the corporate practice of other

In general terms, Colombian corporate law allows the exclusion of associates (partners or shareholders) as a penalty for the breach of the obligation of paying subscribed shares or quotas in the legal or agreed term. Nonetheless, the exclusion of the breaching associate is only one of the three options that the Company can take, which includes, (i) forcing the payment, and (ii) reducing the contribution to the paid shares or quotas minus a penalty of 20%. Likewise, in accordance with articles 101 and 104 of the Colombian Code of Commerce, an associate’s quality of partner or shareholder ceases if there are vices in the execution of the incorporation act (e.g. defect in capacity or lack of power), or in the agreement or act by which he acquired such quality.

In the case of partnerships, Colombian law provides for a number of cases in which the exclusion of partners is allowed, but then again, these cases also respond to sanctions imposed by the law for very particular and limited events. Exempli gratia, in compliance with article 297 of the Colombian Code of Commerce, the partners of a General Partnership (Sociedad Colectiva) may squeeze out a partner who either performed, directly or indirectly, the same business as the company, or acquired an equity participation on a company with the same corporate purpose as the company, without prior consent of the remaining partners. Likewise, article 298 of the Colombian Code of Commerce gives power to the board of partners of a General Partnership to squeeze out any partner who unlawfully withdraws any of the company’s assets, or uses the firm’s name for his personal business.

In the case of the Limited Liability Company (Sociedad Limitada), the Superintendence of Companies has stated that, apart from the cases established in the law for the exclusion of

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87 Colombian Code of Commerce, Article 125.
partners of this type of company, the events provided by law for the exclusion of partners on a General Partnership are also applicable if—and only if—provided for in the bylaws. Likewise, article 365 of the Colombian Code of Commerce allows the partial dissolution of the company when a partner voluntarily retires and the remaining partners do not acquire the retiring partner’s quotas, nor allow their acquisition by a third party.

As to the possibility of establishing special rules for the exclusion of partners in either a General Partnership or in a Limited Liability Company, Francisco Reyes Villamizar, states that in both these types, the possibility of exclusion by means of provisions in the bylaws is derived from the intuito personae nature of partnerships. This interpretation seems to be supported in (i) article 358 of the Colombian Code of Commerce, which gives the board of partners the power to decide over the appraisal right and exclusion of partners; and (ii) paragraph 14 of article 110 of the Colombian Code of Commerce, which allows partners to agree on any rule in the bylaws as long as it is compatible with the company’s type nature. Moreover, the Colombian Superintendence of Companies has sustained that in order to carry out the exclusion of a partner of a Limited Liability Company, and whenever there is a legitimate motive for such exclusion, the company has to take into account the appraisal proceeding provided for in the Colombian Code of Commerce.

Nonetheless, it is important to consider that most exclusion clauses are, by nature, sanctions imposed by law; therefore, the powers awarded to individuals to establish exclusion clauses, other than those provided for in the Colombian Code of Commerce, should be very limited. Likewise, it is important to consider that the exclusion of a partner necessarily implies a

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diminution of the stakeholders’ equity in quantity, and in its quality as a general security interest of the company’s creditors. These, among other arguments, have led the Colombian Superintendence of Companies to adopt a more conservative approach, which tends to deny absolute freedom in relation to the establishment of exclusion clauses in the bylaws, other than those already provided by law.\footnote{Superintendence of Companies. Concept No. 220-070501 of 2015.}

The regulation of General Partnerships is applicable in the case of the managing partners (socios gestores) of the Limited Partnership (Sociedad en Comandita Simple); while the regulation for the Limited Liability Companies is also applicable to the limited liability partners of the Stock Partnership (Comandita por Acciones).

As to the Stock Corporation, other than the exclusion provision of article 125, in accordance with the doctrine of the Colombian Superintendence of Companies, even when neither the Code of Commerce nor Law 222 provide for an express prohibition, in light of the rule of paragraph 14 of article 110 of the Colombian Code of Commerce, and the capitalistic nature of this type of company, the establishment of shareholder exclusion clauses in the company’s bylaws is incompatible with the Stock Corporation, especially considering that it is based on equity contributions and not in the special features or character of its shareholders. Capital partners of the Stock Partnership are governed by the rules of the Stock Company.

3.2. Squeeze outs regulation – Appraisal and Sell-Out Rights

The Colombian institution from the classic corporate regulation most similar to a squeeze out regulation is the appraisal or sell-out right\footnote{We will refer to the institution known as “Derecho de retiro” as either sell-out right or appraisal right. This name is given because it is generally a right awarded to shareholders under certain conditions to force the purchase of their shares by either the remaining shareholders or the company (sell-out), but when it comes to the establishment of the rules of the company, it tends to deny absolute freedom.} awarded to every shareholder in certain very
specific cases.

Article 12 of Law 222 of 1995 provides for a sell-out right in favor of absent or opposing shareholders and partners whenever (i) a merger, transformation or spin-off implies a worsening of their economic rights, or an increase in their scope of liability, or (ii) whenever a public company goes private. Moreover the same article establishes that a “worsening of a shareholders’ economic rights” means: (i) a decrease in the equity participation of such shareholder in the company’s stockholders equity, (ii) a decrease on the equity value or nominal value of the share or quota (only if it is a consequence of a diminution of capital), or (iii) a limited or decreased share negotiability. In the case of the Simplified Stock Corporation (Sociedad por Acciones Simplificada), there is a third scenario for the exercise of the sell-out right, which, in the terms of article 31 of Law 1258, is the event of global transfer of assets; this is, whenever the shareholders meeting decides in favor of transferring assets and liabilities representing 50% or more of the total liquid equity of the company.

Please note that an opposing shareholder is only that who has voted against a decision, and never a shareholder who abstained from voting. Additionally, an “absent shareholder” is that who did not assist the shareholders meeting that approved the transaction and thus does not have enough information on the transaction.

In a similar fashion to Section 626 of Delaware’s General Corporation Law, article 13 of Law 222 provides that unless the summoning of the shareholders meeting in which the merger, transformation or spin off (from now on a “transaction”) is to be approved, expressly contains a mention to the power of the shareholders to exercise their sell-out right in the terms of applicable law, such summoning shall be null and void.

amount of consideration, the impossibility of an agreement gives the sellers the right to demand a definitive and compulsory appraisal before the Chamber of Commerce.
The aforementioned absent or opposing shareholders have eight days from the date of the shareholders meeting in which the transaction was approved to deliver in writing a notification expressing its intention to sell-out. Within the following five days, the company shall make an offer of such associate’s shares or quotas to the remaining shareholders or partners, and if such remaining shareholders or partners do not acquire the offered shares or quotas, all or part, the company shall re-acquire them, if possible. In the event that there are shares or quotas that are not purchased by either the remaining associates or the company within the 10 days following the sell-out notice, such shareholder or partner requesting the sell-out can demand the reimbursement of its equity contribution for the remaining shares or quotas.

The sell-out or appraisal right is conceived as a protection for minority shareholders before transactions that have the potential to negatively affect their standing in a company, therefore the nullity of any stipulation against it. As in most systems, in the corporate context the decisions adopted by the corporate organisms are compulsory for all the shareholders or partners, even when they are against such decisions. The sell-out right exists on the ideal of giving the shareholders an easy exit when certain decisions may cause economic damages or risks to such shareholders. However, as evidenced in rulings of the Colombian Superintendence of Commerce\textsuperscript{93}, the sell-out right is sometimes used along with abusive or aggressive methods such as a blockage to the distribution of utilities by majority shareholders, as a way to force the exit of minority shareholders. This illegal practice has the same effects as a squeeze out, but is performed with methods than constitute an abuse of rights\textsuperscript{94}.

The sell-out right provided in Law 222 can only be used in very specific cases that may

\textsuperscript{93} In Colombia, the Superintendence of Companies has judicial powers, and therefore acts as specialized corporate and insolvency judge in certain scenarios.

\textsuperscript{94} Superintendencia de Sociedades. Sentencia S. 800-44. Isabel Cristina Sánchez Beltrán contra Centro Integral de Atención del Infractor de Tránsito S.A.S., Jeny Marcela Cardona y Juan Carlos Cardona.
not cover all the possible scenarios in which a transaction may affect the minority; thus, if a shareholder cannot prove or argue an economic damage or an increase in liability (in the terms of article 12 of Law 222), selling out is not an option.

In fact, even when Professor Reyes sustains that the sell-out right exists for those associates that, due to the changes of circumstances lose interest in staying in a company, Professor Luis Alfonso Mora states that by means of protecting the stability of the company, the application of the sell-out right is made so difficult that “The sell-out right, as provided in our legislation, seems ineffective due to the many obstacles and demands to which its exercise is subject. Likewise, there are only a few causes for its exercise, making it of rare occurrence”.

Other authors like Enrique Gaviria Gutierrez argue that even when the principle of company preservation is of utmost importance, its protection cannot go against the protection of the equality-based rights of certain shareholders, without, of course, promoting a tyranny of the minority.

As per consideration, Law 222 seems to be more protective of the selling partners or shareholders. In the events of purchase and re-acquisition of shares, consideration is to be determined either by the method agreed in the bylaws, or by a private agreement between the parties. If such agreement is not reached, the parties shall rely on the appraisal of a qualified expert appointed by the Chamber of Commerce of the company’s residence city. The same methods shall be used in the event of a reimbursement of shares.

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Nonetheless, the first obstacle shareholders face when exercising a sell-out right might be the reluctance of the remaining shareholders to acquire the offered shares. Also, the possibility of the company purchasing the offered shares is limited by the amount of the company’s reserves for re-acquisitions. The third obstacle a shareholder in the use of its sell-out right might encounter is the regulations for the reduction of capital. A company cannot reduce its capital unless (i) it does not have any external liabilities, (ii) after the reduction the company’s assets, its capital shall at least double the external liabilities, or that (iii) the company’s creditors approve of the reduction, whatever the assets of the company. Additionally, even if the company were to comply with the aforementioned requisites, it still has the possibility of claiming financial impossibility or difficulties to delay or even get a declaration of inadmissibility on the payment, which might make reimbursement almost impossible.

Finally, as was studied in the first section of this paper, sell-out rights are related but are not equal to squeeze outs. The sell-out and appraisal mechanism of Law 222 does not allow a shareholder to force the exit of the remaining shareholders, but allows minority shareholders to exit when conditions turn unfavorable. Therefore, sell-out rights as currently contemplated by Colombian law do not properly address the economic issues that are addressed by squeeze out regulations around the world. As will be analyzed ahead, we believe that the only way to perform a proper squeeze out in the traditional companies of the Colombian Code of Commerce might be through shareholders agreements, though, as we will study further below, this might also offer some obstacles.

3.3. Law 510 and the constitutional protection of share ownership

Almost four years after Law 222 was enacted, the congress enacted Law 510 on the
financial and insurance system. Article 70 of Law 510 contained a rule which allowed the shareholders assembly of public companies to squeeze out shareholders who, for a period of 20 years, failed to exercise their rights under applicable laws and the company’s bylaws.

Article 70 reads:

“To the owners of shares listed in the National Securities Registry, and in one or more Stock Exchange in the country, that for a 20 year term have not exercised any of the rights granted to them by the law or the corporate bylaws, the company shall, prior approval by the shareholder’s general meeting, reacquire their shares by depositing the corresponding price, in accordance with the equity value of the share from the last accounting exercise before the reacquisition, in an account in favor of the shareholder(s)”98

Unfortunately, ten years later Colombia’s Constitutional Court, on Ruling C-133 of 2009, ruled against the constitutionality of article 70 of Law 510 sustaining that, in addition to denying any defense to the squeezed shareholder, it was a violation to the right of private property and could not be enclosed into any of the constitutional exceptions or limitations to such right.

a. The right to private property

The Colombian Constitutional Court found that in accordance with the Colombian Constitution every interest, be it public or private, shall serve the community, promote general prosperity, and guaranty the effectiveness of constitutional rights, which includes ensuring the

98 Original text: “A los poseedores de acciones inscritas en el Registro Nacional de Valores y en una o más bolsas de valores del país que durante un término de veinte (20) años no hayan ejercido ninguno de los derechos consagrados en la ley o en los estatutos sociales, la sociedad podrá, previa aprobación de la asamblea de accionistas, readquirir sus acciones consignando el precio que corresponda, de acuerdo con el valor patrimonial de la acción al último ejercicio contable anterior a la readquisición, en una partida a disposición del o los accionistas”.
participation of anyone in decisions that may affect them. Furthermore, the Colombian Constitution protects and guarantees the right to private property, which is why only constitutional level provisions may limit such right, and the law may therefore, only regulate such limitations.

Constitutional limitations to private property include the social and environmental purposes of property, which are related to the non-absolute nature of private property, and the events of expropriation and extinction of ownership.

As per the case of expropriation, article 58 of the Colombian Constitution provides that expropriation is only plausible in cases of social interest or public utility, and compensation has to be paid to the owner of the expropriated assets. Expropriation follows strict procedural rules, and compensation is first negotiated by the State and the owner; if an agreement is not reached, fair compensation is to be determined by a court.

On the other hand, extinction of ownership is limited to cases or illicit or illegal title of ownership, and, as in the case of expropriation, has to follow the rules of due process. Similarly, seizure is a sanction –prohibited by the Colombian Constitution – which implies the loss of property in favor of the State as a consequence of felony, and therefore is subject to a criminal ruling.

As found by the Constitutional Court, property, as a right, is (i) a complete right, as it has a number of attributions (ius fruendi, ius utendi, ius abutendi) of autonomous exercise; (ii) exclusive as it opposes any intromission by third parties, (iii) perpetual as it exists for as long as the asset or thing exists, (iv) principal (as opposite to accessory) and autonomous, (v) irrevocable, as it generally may only be transmitted by the owner’s will, and (vi) a right over things.

Moreover, the court upheld that, as found in previous rulings, limitations to the right to
private property cannot infringe the main core of such right, which is comprised by the minimum degree of exercise of the \textit{ius utendi} and the \textit{ius abuttendi} attributes, that allow its titular to receive an economic utility.

\textit{b. The right to due process}

On the other hand, Colombian Constitution also protects the right to due process as a fundamental right on judicial and administrative proceedings, as well as proceedings of any other nature. The right to defense is intrinsically part of the right to due process.

In compliance with due process, neither the law nor the individuals may establish proceedings that could violate fundamental or constitutional rights. In compliance with the right to defense, any person has to be given an opportunity to be heard and expose its reasoning and arguments, as well as contradict any evidence presented against him/her.

\textit{c. Why was article 70 of Law 510 contrary to the constitution}

Ownership over shares has the aforementioned features and attributions, and thus is subject to constitutional protection. Moreover, the limitation to property established in the sued provision did not have any constitutional backup nor was it based in any of the constitutional limitations to property. Moreover, article 70 of Law 510 did not provide defense mechanisms for the squeezed out shareholder, thus, it did not comply with due process.

The only legal possibility that public companies had to squeeze out shareholders who represented obstacles for the company was taken out of the Colombian legal system, in a ruling that could very well be applied to any squeeze out method that does not provide for a mechanism that allows squeezed out shareholders to either force their stay, or get some kind of involvement in the compensation to be received for their shares.

However, due to the limited and specific scope of article 70 and the absence of protective
rights for the minority shareholders thereunder, we believe Ruling C-133 of 2009 does not represent a general precedent against well balanced squeeze out provisions that may in the future be enacted in Colombia.

3.4. The Simplified Stock Corporation and the evolution of Colombian corporate system

As previously stated, in 2008 the Colombian congress enacted Law 1258 and created the Simplified Stock Corporation, which represented a revolution and a huge advance in Colombian corporate law. This type of corporation included many advances and developments from other jurisdictions, particularly from the United States of America, that were necessary for Colombian corporate law to adapt to new business models, and the new needs of the corporate market.

The Simplified Stock Corporation gave shareholders wide faculties and freedom in the determination of multiple matters on the bylaws, from the possibility of establishing an undetermined corporate purpose and duration, and even eliminated the requisite of plurality of shareholders, to the establishment of wide freedoms in respect to shareholders agreements and shareholder exclusions. Additionally, the abbreviate merger mechanism of article 33 provides for a squeeze out merger mechanism which we will analyze ahead.

To date, this type of company provides multiple options for shareholders to perform squeeze outs, with the shareholders even having the possibility of establishing exclusion causes in the company’s bylaws. The application of these exclusion causes shall be made in consideration of the reimbursement rules provided for the sell-out right cases, in the terms explained before. Additionally, shareholders can establish on the bylaws the proceeding rules for exclusion, but, in the absence of rules on the bylaws, article 39 of Law 1258 provides that the exclusion of any shareholder shall be approved by the shareholders general meeting by a plural

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number of shareholders, with a majority of 50% +1 of the represented shares, without the vote of the excluded shareholder.

More importantly, articles 30 and 33 of Law 1258 authorize mergers where shareholders of the merging Simplified Stock Corporation can be compensated with cash, any type of asset, and even shares of other companies. The aforementioned article 30 refers not only to mergers, but also to spin-offs, thus allowing the company to cash out shareholders from any of the resulting companies.

After providing that any transaction on a Simplified Stock Corporation shall follow the rules of the Stock Corporation, article 30 of Law 1258 establishes:

“PARAGRAPH. Shareholders from the absorbed or span-off companies can receive cash, shares, quotas or equity titles in any Company or any other asset, as sole consideration on the merger or spin-off transactions carried by a Simplified Stock Corporation.”

Thus, opening a path for a broad spectrum of possibilities for transactions in which the controlling shareholder whishes or simply needs to squeeze out minority shareholders in a Simplified Stock Corporation. Nonetheless, there seems to be multiple relevant issues that the law left unanswered. Firstly, article 30 seems to imply that any shareholder may be squeezed out in a transaction, but it does not set any requirements for establishing if just any shareholder can be squeezed out or if the squeeze out has to obey certain motives; this situation, together with the fact that the law does not seem to provide specific rules as to the methods to establish the amount

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100 Original text: “PARÁGRAFO. Los accionistas de las sociedades absorbidas o escindidas podrán recibir dinero en efectivo, acciones, cuotas sociales o títulos de participación en cualquier sociedad o cualquier otro activo, como única contraprestación en los procesos de fusión o escisión que adelanten las sociedades por acciones simplificadas.”
of consideration, creates concerns in relation to minority rights and the possibility of abuse of majority.

For instance, following article 30’s remission to the rules of the Stock Corporation, article 173 of the Colombian Code of Commerce provides that the merger shall be approved by the shareholders general meeting with the quorum and majority established on the bylaws. Then, the merger project shall be approved by 50% +1 of the shares represented in the shareholders relevant meeting, unless the bylaws provide for a higher quorum or majority. The same rule applies for a spin-off if we follow article 4 of Law 222. In the same meeting, shareholders shall approve the merger project previously prepared by the company’s administration; such project shall include the terms of exchange\textsuperscript{101} of the transaction, which in the case of a Simplified Stock Corporation should also establish the type and amount of consideration of any squeezed out shareholders. Then, if the project and the transaction itself are to be approved by a simple majority in the shareholders meeting, minority shareholders would not be generally able to oppose either the transaction, the terms of exchange, nor the consideration they are to receive.

Nonetheless, the question of whether such consideration has to follow the rules set for the sell-out right in Law 222 remains. Of course, as in the case of any other types of company, any shareholder who was absent or opposed during the meeting in which the transaction was approved, has the faculty of exercising a sell-out right, so, for instance, it does not make much sense to apply sell-out right rules to squeezed out shareholders. Naturally, one would think that any consideration awarded to squeezed out shareholders should be higher than the price or reimbursement paid to a retired shareholder, mainly because reimbursement cases tend not to be free of conflict, and thus the price is usually fixed by an auditor on a market basis, while cash out

\textsuperscript{101} Paragraph 4 of article 173 of the Colombian Code of Commerce, and paragraph 5 of article 4 of Law 222
transactions generally involve prior negotiations, and the controlling shareholder wants the transaction to go as smoothly and riskless as possible.

On this point, the Colombian Superintendence of Companies has argued that given that the cash out implies an effective reimbursement and an consequent diminution of the stakeholders’ equity, the rules of the reimbursement and retirement compensation shall be followed in the cases of cash out mergers and abbreviated mergers in a Simplified Stock Corporation\textsuperscript{102}. Additionally, as established in article 86.7 of Law 222, the terms of exchange of a cash out merger –since technically it implies a contribution reimbursement– are subject to prior authorization by the Superintendence of Companies\textsuperscript{103}.

Given that there is no requirement as to the motivations for the squeeze out, as long as the transaction is made at arm’s length, the consideration awarded to squeezed out shareholders is fair (i.e. respects at the very least market prices), and the transaction does not fall under majority abuse of rights, a squeezed out shareholder will likely have no grounds to initiate any administrative or judicial proceeding claiming damages, a fairness opinion, or even the annulment of the transaction before the Colombian Superintendence of Companies.

The Colombian Superintendence of Companies has judicial powers to interfere on events of illegal decisions, abusive acts or decisions, or acts of conflict of interest; and has enough powers to suspend and annul the Minutes of any meeting in which such acts or decisions were approved.

As per cases of abuse of rights, the case law of the Colombian Superintendence of Companies has studied multiple cases of abuse of the rights of vote and abuse of majority, and has established a test to determine whether such abuse exists in a particular case. This because, as sustained by the Colombian Superintendence of Companies, the complexity of the corporate

\textsuperscript{102} Superintendencia de Sociedades. Concept No. 220-172858 of 2011.
\textsuperscript{103} Superintendencia de Sociedades. Concept No. 220-064342 of 2015
world makes it hard to determine abuse situations only with the analysis of compliance with the laws or the contract; in the investigation of abuse of rights cases, it is compulsory to make a careful analysis of the circumstances surrounding the claims, as well as the relations and the behavior of the shareholders.\textsuperscript{104}

Thus, the abuse of rights test performed by the Superintendence of Companies based on article 43 of Law 1258 analyzes (i) whether or not there was a breach to the law or the company’s bylaws, (ii) the effects of the decisions and the effects of the way such decisions were taken, (iii) the existence of conflicts among the shareholders, and (iv) the intention to either inflict damage to the affected shareholders or achieve an unjustified benefit.\textsuperscript{105} It is this last requisite that makes it very burdensome, at least as per obtaining and collecting evidence, for the squeezed out shareholders to have a solid successful case on their part, if they want to reverse the transaction or even claim damages.

As per the case of the abbreviate merger, article 33 of Law 1258 provides that any company with the ownership of an equity interest of more than 90% of a Simplified Stock Corporation can absorb such company with the sole requisite of a decision on the board of directors or legal representative of both companies. The legal representative’s approval would, of course, only be sufficient in the case of a Simplified Stock Corporation that does not have a board of directors.

Sell-out rights are also applicable in the case of article 33 of Law 1258, even though there is in fact no shareholder meeting for the approval of the merger, and thus there cannot be any

\textsuperscript{104} Superintendencia de Sociedades. Sentencia S.800-0073. Serviucis S.A. contra Nueva Clínica Sagrado Corazón S.A.S. Also in Superintendencia de Sociedades. Sentencia S.800-000020. Capital Airports Holding Company contra CAH de Colombia S.A.

absent nor opposing shareholders. To clarify this point, the Colombian Superintendence of Companies has understood that in the absence of a shareholders general meeting, every shareholder is to be considered absent and thus, every shareholder can exercise the sell-out right in the terms of Law 222\textsuperscript{106}. On the day that the abbreviate merger is decided, the decision shall be communicated to the shareholders, and from then starts the 8-day term for the exercise of the sell-out right.

Finally, in the case of the abbreviated merger, administrators have to be careful in appropriately complying with their fiduciary duties before the company and the shareholders. The core of Colombian Law on the fiduciary duties of directors and officers is contained in section 23 of Law 222. The three main features of this statute are the following: (1) fiduciary duties are owed to the company, “considering the interests of its shareholders”; (2) directors must perform their duties “in good faith, with loyalty and with the care of a good businessman”; and (3) directors and officers are under specific duties to (a) take action to fulfill the company’s purpose, (b) procure compliance with the law and the company’s corporate documents, (c) allow the corporation’s fiscal auditors to comply with its duties, (d) protect the company’s trade secrets, (e) refrain from improperly using privileged information, (f) treat all shareholders equally, (g) abstain from competing with the corporation, and (h) abstain from taking part in conflicted transactions.

As for the compensation and the terms of exchange, the short-form merger authorizes the parent company to compensate the shareholders of the absorbed subsidiary with cash, assets, or shares of any other company, and not necessarily shares of the parent company, thus, short-form mergers are also a possibility for squeeze outs in Colombian law.

\textsuperscript{106} Superintendence of Companies. Concept 220-048575 of 2012.
3.5. **Shareholder agreements and the possibility of private squeeze out regulation**

Shareholders agreements offer opportunities for shareholders to make private arrangements on conditions or rules which inclusion in the company’s bylaws may not be authorized by law. Nonetheless, the rules for shareholders agreements vary substantially within the traditional companies of the Colombian Code of Commerce and a Simplified Stock Corporation.

Article 70 of Law 222 establishes the general rules for shareholders agreements on a Stock Corporation. This provision is also applicable to the Limited Liability Company and the Stock Partnership by express remission of the Colombian Code of Commerce.

In compliance with the aforementioned article 70, two or more shareholders may execute agreements to vote on the same or in a determined way, and even to allow one or more of them to represent the rest on the shareholders general meeting. Moreover, for such agreement to be enforceable before the company it shall be deposited on the company.

As analyzed by Sergio Michelsen and Dario Laguado, article 70 of Law 222 has divided doctrine in two about the enforceability of shareholders agreements: (i) a minority that upholds that shareholders agreements are only enforceable before the company on what is related to voting and representation agreements, while the rest of the agreement is only enforceable between the executing shareholders; and (ii) a group that argues that shareholders agreements are fully enforceable.¹⁰⁷

Article 70 provides:

“Two or more shareholders, who are not administrators of the company, may execute

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agreements by which they agree on voting in the same or a determined way in the shareholder meetings. Such agreement may include clauses that allow one or more of them, or third parties, to represent all of them in one or all shareholders meetings. This clause shall have effects before the company whenever it is in written form, and is delivered to the legal representative for its deposit on the headquarters of the company. As for the rest, neither the company nor the remaining shareholders are liability for the breach of the agreement”.

The limited enforceability faction sustains its opinion in an interpretation based on the last sentence of the provision on article 70, dividing the provision in two: (i) voting agreements, and (ii) representation agreements; and limiting enforceability to the second type of agreements if they are not in written form and deposited in the company\textsuperscript{108}.

Contrary to this opinion, the full enforceability faction considers that any shareholder agreement complying with the requisites of article 70 – that is, it is in written form, and is delivered to the legal representative for its deposit on the headquarters of the company – is fully enforceable before the company and the remaining shareholders. Nonetheless, it cannot be denied that such full enforceability can only refer to voting and representation agreements, as upheld by the Colombian Superintendence of Companies in recent concepts, stating that “As to the remaining company types article 70 of Law 222 of 1995, provides that shareholders agreements can relate exclusively to voting and the person to represent the parties in shareholders meetings. (...)”\textsuperscript{109} Nonetheless, it does not imply that such other agreements are prohibited for the

\textsuperscript{108} Ibidem, Page 19.

\textsuperscript{109} Superintendence of Companies. Concept No. 220-071420 of 2015. Original text: “Respecto de los otros tipos societarios el artículo 70 de la Ley 222 de 1995, dispone que los acuerdos de accionistas pueden versar exclusivamente sobre el sentido del voto y, acerca de la persona que representará a los firmantes en las reuniones de la asamblea de accionistas.”
Superintendence of Companies has also upheld that the remaining agreements are enforceable only between the parties to the shareholders agreement\textsuperscript{110}.

On the other hand article 24 of Law 1258 allows shareholders of a Simplified Stock Corporation to execute shareholder agreements on any licit matter. Such agreements shall be deposited on the company, and have a duration of no longer than 10 years (which can be indefinitely extended by periods of 10 years), to make them enforceable before the company, which means that (i) any vote issued in breach of the deposited agreement shall not be computed and that (ii) shareholders may claim the performance of any obligation and covenant established on such agreement before the Colombian Superintendence of Companies.

Any controversy in relation with the compliance or breach of shareholders agreements and the clauses established in such agreements can be taken before the Colombian Superintendence of Companies in accordance with the provision on article 24 of the Colombian General Code of Judicial Procedure.

Shareholders agreements may not involve the company itself, but through them shareholders have found mechanisms to achieve what corporate regulations limit. For instance, on a shareholders agreement parties can establish a call option which, under certain agreed requirements, allows one of the executing shareholders to force the remaining ones to sell their shares, allowing him to purchase them under pre-established conditions at its will.

Another clause that allows a controlling shareholder to squeeze out minority shareholders is what is usually known as drag along rights. Through a drag along, a majority shareholder selling its stake in the company can force the remaining shareholders to join him in the sale, thus leaving the purchaser as the sole shareholder. As described by Dario Laguado and Sergio

Michelsen:

“Through a drag along right, the controlling shareholder avoids any opportunistic behavior from the minority shareholders that may hinder this type of transaction [the acquisition of 100% of a company] with the veiled purpose of extracting value from the controlling shareholder. (...) a drag along right produces a positive signaling effect before potential buyers”\textsuperscript{111}

Deadlock provisions, such as Russian Roulettes and Texas Shoot-out clauses, are also squeeze out options that may be agreed on in shareholders agreements. These clauses are known in Colombia as “\textit{voy o van}” and are commonly used in the events of conflicts among shareholders, or even situations in which the shareholders general assembly gets blocked due to shareholders disagreements. In compliance with this clause, one or more of the agreement’s parties has the right to make a compulsory offer to the remaining parties, upon which the recipients may either accept the offer and sell their shares, or purchase the shares of the offeror, thus eliminating the conflict and squeezing out “unwanted” shareholders.

Consequently, shareholders agreements represent a feasible mean to establish squeeze out mechanisms under Colombian law, especially on the traditional companies of the Code of Commerce, even if they cannot be made enforceable by the company itself.

3.6. \textit{Bill 70 of 2015: another step towards freedom on corporate forms}

In light of the proved benefits and positive effects of Law 1258, on 2013 senator Simon Gaviria presented before the Colombian congress a Bill 145 of 2013 which was directed towards

\textsuperscript{111} Michelsen, Sergio Pablo y Darío Laguado Giraldo. Op Cit. Page 7. Original quote: “\textit{Mediante un derecho de arrastre, el accionista controlante evita que los accionistas minoritarios puedan comportarse de manera oportunista, entorpeciendo este tipo de transacciones con el velado propósito de extraer valor del accionista controlante. (...) un derecho de arrastre produce un efecto positivo de señalización (signaling effect) frente a potenciales compradores}.”
applying many of the regulations of the Simplified Stock Corporation to the companies of the Colombian Code of Commerce. Unfortunately, the bill was not successful and did not pass.

On 2015, the Colombian Superintendent of Companies, professor Francisco Reyes Villamizar together with the national government filed a bill that is directed towards “continuing the modernization and softening of the corporate regime”\textsuperscript{112} by updating the regulation of the companies on the Colombian Commercial Code with the application of some of the most positive rules of Law 1258 by working on the premise of party autonomy.

The purpose behind the bill, in the terms of its explanatory memorandum, is “to provide entrepreneurs with the most advanced legal tools for the undertaking of any type of business, particularly in the context of the “closed” companies, this is, those whose securities are not traded in the Stock Exchange.”\textsuperscript{113}

In fact, paragraph 7 of article 4 of Bill 70 provides for the application of article 39 of Law 1258 (which allows the establishment of exclusion clauses on the bylaws) in the companies of the Colombian Code of Commerce, prior amendment of the bylaws with the approval by 100\% of the shareholders or partners.

Though the Bill does not provide for the application of cash out transactions, the possibility of establishing squeeze out mechanisms in the bylaws would offer easy ways for companies and shareholders to squeeze out free-rider shareholders, problematic shareholders, and even those shareholders who pose obstacles in the normal functioning of companies.

4. CONCLUSIONS

Squeeze out regulations are most important in a corporate context in which company

\textsuperscript{112} Exposición de motivos Proyecto de Ley 70 de 2015. Page 3.
\textsuperscript{113} Ibidem. Page 3.
control is usually concentrated and low float rates are the rule. These regulations, if appropriately balanced, offer solutions for facilitating certain business decisions and certain transactions that are globally positive, while at the same time protecting the rights of minority shareholders.

An effective squeeze out regulations effectively impedes situations of abuse of rights of majority and creates an investment environment that is perceived as safe for minorities by guaranteeing their rights and certain stability for their investments, while also offering opportunities for controllers. Such regulation is achieved by establishing appropriate ex ante control mechanism, such as in the case of the Canadian plan of arrangement, and/or appropriate ex post remedies, such as the entire fairness review in the State of Delaware.

Squeeze out regulation might be one of the pillar stones for countries to fight against controlling shareholders abuses. Most times, heavy regulation and prohibition leads to further abuses from controlling shareholders, and squeeze outs being performed on illegal terms. This is the case in Colombia where, as seen, controlling shareholders may aggressively use their prerogatives to force the exit of the minority shareholders, forcing them to make use of their sell-out rights.

On the other hand, it is important to note that the Colombian Legal System provides both regulation extremes. On one hand, the companies regulated under the Colombian Code of Commerce and Law 222 have a prohibitive regime, that restricts shareholder freedom in many aspects, among them, the possibility of performing squeeze out transactions.

Contrary to the Colombian Code of Commerce, Law 1258 provides for squeeze out mechanisms like cash out mergers and the possibility of incorporating shareholder exclusion clauses in the bylaws, however, the law does not offer real protections for the squeezed out shareholders, neither on procedural matters nor in price fairness.
What we propose, is an intermediate regulation that would allow duly justified squeeze outs under certain conditions that balance (i) the ability to cash out minority shareholders when that decision is in the best interest of the company under a sound business judgment and (ii) the rights of minority shareholders to a fair process and a fair price or consideration. We believe that such regulation may be facilitated by *ex ante* or *ex post* judicial review, as long as such judicial review is made on the basis of business standards and by duly qualified judges, such as the special court for corporate matters of the Colombian Superintendence of Companies.
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