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Shareholders Meetings as Organs of Corporate Governance in Ethiopia

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ABSTRACT

Shareholders are normally owners of the corporation's assets and the fact that such assets are controlled by the management body is the cause for many of the problems dealt by corporate governance. Shareholders meeting as management organ can play sizeable roles in corporate governance. The problem addressed by this article is therefore what necessary measures can further strengthen the shareholders controlling mechanisms on the corporation upon which they invested their capital. Even though there are many theories concerning their roles in corporate democracy, none of them seem to win the battle. The query of the paper is how to enhance role of shareholders in corporate governance. The paper mainly uses doctrinal research method. Therefore the rules governing shareholders meetings should be well designed in a way of enabling them play their part. It may include access of electronic voting, possibility of voting by mail, facilitating sufficient information disclosure mechanisms, adopting advisory voting and the rules necessary to such vote, facilitating easy exit mechanism to shareholders dissatisfied by majority holders, introduction of stock exchange market could enhance shareholders governance role. Moreover possibility of derivative suits by shareholders is also another mechanism that should be available to them to promote control.

Introduction

1. Corporate governance in general

1.1. What is corporate governance?

We have to bear in mind that most of the time definitions for terms in social sciences are not hard and fast. The same can be true when we attempt to define corporate governance. However for the purpose of this term paper the author tries to adopt the definition used by the Organization of Economic Coordination and Development (from now onwards OECD) and some other authorities. Different authors defined corporate governance on their own ways. For instance Fekadu Petros define it as the notion that refers to the overall legal, institutional and regulatory framework in which the interests of stakeholders surrounding companies are coordinated and protected.[1] Therefore we can note that the concept is all about the mechanisms through which corporation is directed and controlled.

"Corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals…the aim is to align as nearly as possible the interests of individuals, corporations and society."[2] From this we can bear in mind that corporate governance involves various competing interests. The President of the World Bank, Jim Wolfensohn, once said that "[t]he proper governance of companies will become as crucial to the world economy as the proper governing of countries". Proper governance is hence highly related with the world's economic performance.[3]

Corporate governance refers to the system through which the behavior of a company is monitored and controlled. The significance of corporate governance is that in modern economies large corporations are typically associated with a division of labor between the parties who provide the capital (i.e., shareholders) and the parties who manage the resources (i.e., management). Conflict of interest among the two groups might lead to insufficient monitoring of the executive, suboptimal levels of investment in the firm, or some shareholders being expropriated. In these scenarios shareholders might be hurt if there are not sufficient means to ensure that the company is properly monitored.[4]

The fundamental question of corporate governance is how to assure suppliers of finance that they get a return on their investment. But corporate governance is not solely about performance. It is also about the creation and maintenance of a fair and equitable economic relation among investors.

Preamble of OECD Principles of Corporate Governance explains the concept corporate governance as a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined.

[1] Fekadu Petros, Emerging Separation Of Ownership And Control In Ethiopian Share Companies: Legal And Policy Implications, Mizan Law Review, vol 4. No 1. March 2010. P.3

[2] King's report. P. 6

[3] Ethiopian commertial law and trade diagnostic reform. p. 7

[4] Stephen Y.L. Cheung and Bob Y. Chan. Corporate governance in Asia, Asia-Pacific Development Journal, Vol. 11, No. 2, December 2004.pp. 1-2

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It focuses mainly on the problems resulting from separation of ownership and control.[5]

The presence of an effective corporate governance system, within an individual company and across an economy as a whole, helps to provide a degree of confidence that is necessary for the proper functioning of a market economy. As a result, the cost of capital is lower and firms are encouraged to use resources more efficiently, thereby underpinning growth.[6] Corporate governance is one key element in improving economic efficiency and growth as well as enhancing investor confidence.

Corporate governance can be affected by various relationships among participants in the governance system. Controlling shareholders, which may be individuals, family holdings, bloc alliances, or other corporations acting through a holding company or cross shareholdings, can significantly influence corporate behavior. Creditors play an important role in a number of governance systems and can serve as external monitors over corporate performance. Employees and other stakeholders play an important role in contributing to the long-term success and performance of the corporation, while governments establish the overall institutional and legal framework for corporate governance. The role of each of these participants is crucial in corporate governance and their interactions may vary from jurisdiction to jurisdiction.[7]

1.2. Major models of corporate governance

There are two approaches of conferring powers to the board of directors and general meeting of shareholders. They are the "liberal and restrictive" approaches. The liberal approach which is mostly followed by USA legal system is to confer specific power to general meeting such as the power of altering statute of the company, appointment and removal of the directors, and conferring all other powers to the board of directors.[8] This approach refrains from much intervention on the affairs of private contracting parties. It considers firms as standardized contracts.

The restrictive approach on the other hand is to confer the power to the board of directors and general meeting by specifying in the memorandum or articles of association. According to this approach board of directors has limited power. This approach is, adopted by the continental Europe legal system i.e. civil law.[9]

1.2.1.The theoretical foundations of major models

Various views and theories are there concerning the reasons of existence and the ways how firms be governed. These theories have a common thread that they all share and thus we can categorize them based on their common features. Generally the theories seem to fall into the complete contracting (the principal agent) and the incomplete contracting.[10] According to the complete contracting theory the agents to the firm can foresee all the possible future contingencies ex-ante while the incomplete contracting theorists believe that it is not possible to see all the possible contingencies and so ex-post governance is mandatory.[11] Therefore it believes in strong regulation by the government unlike the principal agent or complete contracting theory which gives more freedom to the parties.

Theories of the firm may roughly be classified into two categories:[12]

(a) Incomplete contracting models which are founded on the assumption that it is costly to write elaborate contracts, and that there is therefore a need for ex post governance.

(b) Principal-agent models (complete contracting theories) which allow agents to write elaborate contracts characterized by ex ante incentive alignment under the constraints imposed by the presence of asymmetric information. Here agency theory is considered as a subset of contract theory. The Nexus of Contracts View and Formal Agency Work belong in the complete contracting category.[13]

1.2.2.The diffused Ownership Model

This model is also known as shareholder based model. It is dominant in the Anglo American legal system. The fundamental question of corporate governance here, unlike the concentrated model, is how to assure suppliers of finance that they get a return on their investment. The reasons for preference of a certain structure are explained differently by two polarized views: neo-classical and path-dependent. Neoclassical economists insist that firms choose their corporate structures based on simple efficiency considerations: the most efficient ones are chosen accordingly. Path dependence assumes that corporate governance structures are deeply rooted in countries' historical traditions and initial ownership structures of organizations.[14]

This model has chosen to have a financial system where the power of financial institutions, such as banks and insurance companies, is quite limited. It is mainly based on equity finance and control primarily by capital or stock markets with a characteristic feature of diffused ownership. Dispersed ownership model of corporate governance is characterized by "strong securities markets, rigorous disclosure standards, and high market transparency, in which the market for corporate control constitutes the ultimate disciplinary mechanism"[15] on management.

1.2.2.1. Its implication

In this model there is no such what we call big block holders and surrender by shareholders to controls of management. This is due to problems of coordination and lack of collective action as a result of practical difficulties to do so. Shareholders in a publicly held corporation typically have limited legal right to engage in its day to day management.

[5] OCED Principles of corporate governance, p.12

[6] ibid

[7] Ibid, p.12

[8] Alemayehu Fentaw and Kefene Gurmu, traders and business organization, unpublished, p.120

[9] ibid

[10] Nicoli J. Foss. The theory of the firm: an introduction to themes and contributions. P,19 available at http://www.cassey.com/foss.pdf

[11] Robert axttel, The Emergence of Firms in a Population of Agents: Local Increasing Returns, Unstable Nash Equilibria, And Power Law Size Distributions. Pp,3-4 and see also Foss. P,18

[12] Nicoli J.Foss, theory of the firm available at http://encyclo.findlaw.com/5610book.pdf visited on 8/7/2012

[13] ibid

[14] Geoffrey Owen and etals, Since the 1980s there has been a partial convergence between the shareholder-based and the stakeholder-based systems of corporate governance. What has caused this convergence and is it likely to continue? Pp.2-3

[15]As cited in Fekadu. Petros, p.7, John D. Coffee (2001), "The Rise of Dispersed Ownership: The Role of law and State in the Separation of Ownership and Control," *The Yale Law Journal, 111* # 1, p.3.

Each of the dispersed small holders will thus have little information and much less motivation to monitor the management. Though dispersed small holders can become powerful by coming together, the cost of making such coordinated action is often high. Even voting in which shareholders are expected to be more organized has often been manipulated by the managers to the latter's advantage.[16]

The managers may thus be tempted to using their control over corporate assets to promote their own interests at the expense of that of the shareholders. To the extent that the management pursues its own interest at the expense of the shareholders, it imposes what economists call agency cost.[17]

However, there are mechanisms of minimizing agency cost which are part and parcel of legal systems utilizing this model. First, the labor market for corporate executives has a disciplinary role on the conduct of managers. Managers want to perform well in order to impress potential employers at a better term. Secondly, bad management which sufficiently causes a decline in the market share for products or services can cost management its job. The most effective disciplinary tool in the widely held company however is the third mechanism hostile takeover. Hostile takeover occurs when shareholders unhappy with the performance of their company opt to walk out by selling their shares to a control bidder. If managers perform persistently badly, an outsider may take over by buying a majority of the shares through a hostile takeover i.e., one rejected by managers but accepted by shareholders.[18]

The Anglo-American model has other merits as compared with systems characterized by concentrated ownership.[19]

1. The separation of ownership and control often carries with it the benefit of hiring more qualified managers since executives are hired on the basis of their managerial credentials, than on their ability to finance the firm or their family connections with dominant shareholders.
2. The absence of block holders also creates a convenient working environment for professional managers since small dispersed owners are unable to interfere with the business of the management. Thus, the agency cost problem may to some extent be offset by this benefit.
3. Dispersed ownership brings high liquidity to stock markets and cheapens the cost of capital provided there is a stock market in place. More dispersion results in more liquidity as there will be more market participants. Hence exit is easier for unhappy shareholders. Shareholder migration also plays the role of monitoring management to some extent, since such act of shareholders reflects on the state of the company, and eventually leads its stock prices to fall.
4. Dispersed ownership of stocks has also the economic benefit of distribution of risk, in comparison to the concentrated ownership model where few block holders bear all or most of the risks of businesses.

In some countries, companies employ anti-take-over devices. The OECD Principles of Corporate Governance states that anti-take-over devices should not be used to shield management and the board from accountability. However, both investors and stock exchanges have expressed concern over the possibility that widespread use of anti-take-over devices may be a serious impediment to the functioning of the market for corporate control. In some instances, take-over defenses can simply be devices to shield the management or the board from shareholder monitoring. In implementing any anti-takeover devices and in dealing with take-over proposals, the fiduciary duty of the board to shareholders and the company must remain paramount.[20]

1.2.3.Concentrated Ownership Model

German and Japanese are predominantly using this model. It is mostly used in the continental Europe and Asia and is also known as stakeholder based model. Countries with this paradigm of corporate governance tend to have weak securities markets, and low disclosure and market transparency standards. As opposed to the case in diffuse ownership governance systems, only a modest role is played by the market for corporate control, a greater part of the monitoring role being played by large banks with the dual role of shareholders and major creditors.[21]

A whole set of different groups, such as employees, customers, suppliers and society at large constitute the framework within which the governance should be considered.[22] This approach attempts to insure that the managers meet the interests of both shareholders and also other stakeholders. This system in continental Europe and Asia is associated with concentrated ownership structures. The latter is also known as relationship-based system, meaning that ownership of most publicly quoted companies is in the hands of few long-term committed shareholders, directly involved in governance. The large number of investors here is less prevalent, and the owners are very often represented by families or few individuals.[23]

For instance one study made by Prowse S. reveal that Japan and Germany have respectively 33.1% and 41.5% of outstanding shares owned by the largest five shareholders, whereas in the United States and United Kingdom the figures are as low as 25.4% and 20.9% accordingly.[24]This very statistics clearly show the concentration and the diffusion in the aforementioned models.

An immediate effect of the concentrated ownership model on stock market development seems to be negative. The reason is that large block holders that manipulate corporate power may not easily liquidate their holding or more technically do not change their market positions, negatively affecting liquidity. Secondly, the few small holders cannot create enough liquidity as the volume of stocks on the market will be lower. On the other end of the spectrum, small investors will not be ready to buy shares for fear of domination by block holders. A study comparing Continental stock market practice with that of the Anglo-Saxon concludes that, in Continental models, such as the German and Japanese systems, "stock market liquidity is not an issue . . . Accounting information is often murky. There is only limited protection against insider trading. As a result stock markets play a lesser role than the Anglo-American mode.[25]

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[16] Supra note one P. 8.
[17] Ibid.p 9
[18] ibid
[19] Ibid, p.10

[20] Supra note five, P.36
[21] Supra note one
[22] Supra note 14. p.2
[23] ibid
[24] Prowse, S. (1995). "Corporate governance in an international perspective: A survey of corporate control mechanisms among large firms in the U.S., U.K., Japan and Germany". *Financial Markets, institutions and Instruments*. Vol. 4, pp. 1-63
[25] Supra note 1., pp.12-13

Concentrated ownership tends to reduce agency cost. Block holders will tend to be efficient monitors than dispersed shareholders. To elaborate, controlling shareholders are likely to have a financial stake which is large enough to motivate them to keep a careful watch on what is going on around the company. The other benefit of concentrated ownership is that the presence of large block-holders such as a family yields competitive economic advantages stemming from continuity and long term orientation. In this respect, the Anglo-American dispersed ownership model is criticized for its features of unhealthy orientation towards short term profits. The financial institutions which collectively own much of the equity in American and British publicly held companies have been identified as the primary sources of this bias.[26]

2.1. Shareholders role in corporate governance

Management of a company is structured in to different organs such as shareholders meeting, board of directors and officers of the company. These are mandatory organs for publicly held share companies. General shareholders meeting have a significant place in the management of a company for shareholders have an inherent right to vote in the decision of a company, particularly in the appointment of directors or auditors, decision concerning their remuneration, approval of statement of account decision about dividends and amendment of company constitution.[27] Second board members being appointed by general shareholders meeting have the power to appoint officers of a company and set basic corporate policy where as officers are responsible to run the day to day activity of a company.[28]

From the manager's point of view shareholders often seem a remote body of faceless people to be placated with dividends and soothed by glossy annual reports. The teacher of managerial theory is apt to see the shareholders as one of several groups whose interest must be balanced and bargained out by management. The law, on the other hand, regards the shareholders as the beneficiaries of the corporation, almost its owners, and the objects of management's fiduciary duties and the ultimate sources of corporate power. It gives the two basic weapons with which to enforce that control: the vote and the derivative action[29]…

The ultimate control of the corporation is placed in the hands of the shareholders through those provisions which provide for annual election of directors and for shareholder votes on basic changes.[30] However there is wider gap between the theory and the reality which indicates that such shareholder control is fictional.

After examining the status of shareholders power, commentators declare that it is very low and ask a normative question that is what to do about it? Some of them try to perfect shareholder power, polish up the proxy system or establish separate shareholder standing committee to supervise active managers. Others would proceed to strip the shareholder of what little authority remains to him.[31]

Managerialism is a tendency to believe that corporate power is well located right if it is in the managers. They will tend to balance out the claims of different interest groups fairly if they are left to their own devices free from the pressures of shareholders hungry for dividends.

The other extreme argues that each category of interest group should be given an institutionalized voice somewhere in the corporate structure. It favors a representative parliamentary scheme and placing members from each group on the board.

For my purpose I will set aside the above antagonistic positions in relation to shareholders role in corporate governance and consider their voting exercise and the derivative suits. Voting right is one of the basic rights of shareholders. However it is sometimes legitimate to specify shares with no voting right. Concerning the weight of votes the assumption is not one man one vote, it is rather one share one vote.[32]

Although shareholders as owners of the business are a principal party to corporate governance, some writers hold the view that good corporate governance rests firmly with the board, and auditors and shareholders only play a secondary role. They are of the view that shareholders cannot play a leading role in corporate governance because: firstly, they are subject to financial constraints, are free to buy and sell their shares, and they are not experienced business managers.[33]

Nevertheless, it should be emphasized that shareholders can play a strategic role in enhancing corporate governance if they realize the opportunities provided by annual and other general meetings to exercise their rights for corporate democracy and public scrutiny of directors. It does not require the exercise of specialized or technical knowledge or business experience by the shareholders but merely the exercise of their rights in meetings. Meetings give shareholders direct access to the board, no matter the size of their shareholding.

2.2. Share holders' meetings

Shareholders' meeting can be described as the coming together of persons, who invested their capital in the company, made according to the statutes of the company and the law to discuss matters in relation to the latter. The share holders in meeting are the supreme body of the corporation. A vote of shareholders is normally obtained at a meeting. It is therefore one of the organs that can influence the company's governance and future fate.

2.3. Procedural rules common to meetings

2.3.1.Calling of meetings

In France meetings can be convened by the executive board, the supervisory board, the statutory auditors incase of failure of the board of directors either executive or supervisory, and if the corporation is under liquidation the liquidators. Any interested party in case of urgency or one or more shareholders holding at least one tenth of the issued capital can also apply to the president of the commercial court for the appointment of special attorney to whom the duty to call a meeting is assigned.[34]

As per Ethiopian commercial code meeting may be called by the board of directors, the auditors, the liquidators or by

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[26] ibid

[27] As cited in Mohammed Aliye, Prentice Robert A. Law of Business Organization and Securities Regulation, 2nd ed. Prentice Hall, Englewood, New Jersey 07632, 1994 P. 307

[28] ibid

[29] Detlev F. Vagts, Basic Corporation Law. The foundation press, inc. 1973, New York. P. 352.

[30] ibid

[31] Ibid, p.354

[32] Ibid, pp. 356-357.

[33] Eric Kang Shew Meng, Shareholders' Rights and Responsibilities in General Meetings.

[34] Jean Pierre and Paul More, French Company Law, second edition, Longman Group UK. Ltd, 1992. P. 130

officer of the court. In the case of urgency shareholders holding at least one-tenth of the share capital of the company, can also apply to the court for the appointment of an officer of the court to call a meeting.[35] Moreover the Ethiopian national bank can call a meeting with the view to protect interests of shareholders and depositors of banking business.[36] The bank has strong stake on the soundness and stability of the financial sector.

Meetings can be called by a notice, in a legal newspaper, setting out the name and form of the company, date, times, place and nature of the meeting and the agenda. However, where the company's shares are all registered the publication of notice in legal newspaper is often replaced by individual notice of meeting sent to each shareholder by normal postal service sent by registered letter at the company's expense.[37] Any shareholder may also demand notice to be sent to him by registered letter against payment of an expense where some shares are bearer and others including his own are registered.[38] We can bear in mind that this provision presupposes a commercial gazette which never exist.

At least 15 days must pass the day when the notice of the meeting is published and the date of meeting if a quorum is not present at the first meeting, and at least eight day must elapse between the dispatch of the notice for a new meeting and the date on which such meeting is held.[39]

2.3.2.Setting the agenda

In jurisdictions where the enforcement of the legal and regulatory framework is weak, some countries have found it desirable to strengthen the *ex-ante* rights of shareholders such as by low share ownership thresholds for placing items on the agenda of the shareholders meeting or by requiring a supermajority of shareholders for certain important decisions.[40]Shareholder's holding at least 5 present of the issued capital of the corporation may require resolutions drafted by them to be put on the agenda of a meeting.[41]

The agenda of the meeting is determined by the person calling the meeting. Meetings can only pass resolutions on the questions set out in the agenda. If the meeting has to be called for a second time because a quorum is not present on the first occasion, the agenda cannot be amended for the second meeting. However, meetings may remove any director and appoint other persons to replace them without these matters being in the agenda.[42] Where the national bank calls a meeting as per aricle12 (1, b) of proclamation no 592/2008, it shall prepare the agenda of the general meeting.

Adding more detail to the rules for convening, conducting, and voting at shareholder meetings can promote the latter's control. These include the rules for notice to shareholders, setting the agenda, proxies, quorum requirements, and secret ballots. International experience has shown that these seemingly minor details can be essential to protect the integrity of shareholder control. Consider providing that certain major items require a two-thirds vote, including amending the Memorandum of Association, a merger with another company, a major asset sale, and a decision to dissolve the company.[43]

2.4. Substantial rules common to all meetings

2.4.1.Disclosure of information (the right to information)

Various literatures in corporate governance propose that one of the more immediate needs is to allow investors access to timely and accurate information on the financial and non-financial aspects of the corporations. The following measures to reinforce fair and accurate information disclosure would be relevant. Accounting boards and the audit profession should review the standard and the format in which financial information is disclosed.

2.4.1.1. Assistance of Regulatory bodies

In foreign jurisdictions there are strong and well equipped regulatory institutions that are established to protect the interests of investors of capital in the corporation and other stakeholders. For example the stock exchange is usually the primary regulatory institution concerning the quantity and quality of information disclosed by listed companies. The stock exchange and the other regulatory bodies can work to review and impose whether the information disclosure is sufficient and make changes when necessary.

In a country like Ethiopia where self regulation, absence of trader's code of conduct, is weak or absent such regulator's role is indispensable. Liability should be attached to presentation of irrelevant and falsified information or to the purposive jargons.

In several countries the presentation format of information disclosed is in technical or professional terms that are difficult for the average investor to understand. Stock exchanges and regulatory bodies should work to simplify the language of such information so that investors can have a reasonable understanding of the meaning of the information.[44]

Shareholders are entitled to be given relevant information in advance of any meeting in order to enable them to take fully informed decisions[45]. Before any annual shareholders' meeting, shareholders are entitled to inspect the company's balance sheet, profit and loss accounts, reports of directors and auditors in the three preceding financial years, minutes and attendance sheets of these meetings etc.

The shareholder's inspection rights can be exercised by any shareholder at the company's registered office or main place of business with the assistance of any expert selected.

2.4.2. Right to vote

Many companies in OECD countries are seeking to develop better channels of communication and decision-making with shareholders. Efforts by companies to remove artificial barriers to participation in general meetings are encouraged and the corporate governance framework should facilitate the use of electronic voting in absentia.[46]

Each share carries one vote, and the number of votes which any shareholder may cast at general meetings is calculated accordingly. However, there are certain exceptions to this rule.

- ✓ A company cannot vote on shares issued by it which it has purchased (Art 400)

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[35] Ethiopian commercial code, art. 391
[36] Banking Business Proclamation no 592/2008. Art. 12(1,b)
[37] Supra note 35. art 392(2)
[38] Ibid, art 392(3)
[39] Ibid, art 395.
[40] Supra note 5, p.4o
[41] Supra note 34, P.131
[42] Supra note 35, art 397
[43] Ethiopian commertial law and trade diagnostic reform. P.2
[44] Stephen Y.L. Cheung and Bob Y. Chan. Corporate governance in Asia, Asia-Pacific Development Journal, Vol. 11, No. 2, December 2004. pp. 28-29
[45] Supra note 35, Art. 406
[46] Supra note 5, p. 44

✓The statutes may limit the number of votes which any shareholder may cast, provided that the limitation applies equally to all shareholders (art 408)

✓Where the interest of shareholder conflicts with the interest of the company, such shareholder may not exercise his right to vote (Art 409/1/)

✓Directors may not vote on resolution relating to the directors duties and liabilities (Art 409/3/)

✓The national bank may limit the no of votes by proxy in any meeting of shareholders(Art 13 of proc 592/2008)

✓The voting right of a holder who borrowed money from a bank(Art 13 of proc 592/2008)

Every shareholder's freedom to vote as he wishes is to be respected. Agreements or resolution restricting the free exercise of the right to vote shall be null and void. Shareholder must exercise their voting rights in the collective interests of all the members of the company, and not in order to promote individual is interest.

Resolution of the meeting binds all shareholders whether absent, dissenting or having no right to vote. Courts may decide to nullify a decision of the shareholders meeting when there is evidence that the decision was detrimental to the interest of the company or to the minority or majority shareholders' interests and was dictated only by the self-interest of certain shareholders.

2.4.3.Voting by proxy

Any shareholder may take part in and vote at meetings either personally or by proxy. Where the shareholder appoints proxy, he may not vote personally[47]. The form of the proxy is determined by board of directors. The place and time of deposit of proxy is also determined by the board directors.[48]

A proxy means a lawfully constituted agent. Every member of a company entitled to attend and vote at a meeting of a company is entitled to appoint another person or persons, whether a member or not, as his proxy to attend and vote on his behalf. The proxy shall have the same right as the member to speak at the meeting.[49]

The OECD Principles recommend that voting by proxy be generally accepted. Indeed, it is important to the promotion and protection of shareholder rights that investors can place reliance upon directed proxy voting. The corporate governance framework should ensure that proxies are voted in accordance with the direction of the proxy holder and that disclosure is provided in relation to how undirected proxies will be voted.[50]

2.4.4. Types of Shareholders Meetings

Shareholders meetings can make significant decisions concerning the corporation's future fate. Therefore they constitute considerable organ of the corporation in corporate governance. Hence the meetings are governed by mandatory and non mandatory rules. For instance the corporation's statutes cannot alter quorum and majority requirements.[51]A meeting without fulfilling such requirement is not legally constituted and is not competent to pass decisions.

The shareholders' meeting may be classified as special and general. Special meeting of shareholders, according to Ethiopian commercial law is that meeting among owners of special classes of shares. The general meeting may be ordinary or extra ordinary based on the agenda of the meeting. In these meetings all shareholders regardless of the class of the share they own can participate.

2.4.5.Ordinary general meeting's quorum and majority

As per Art.390, shareholders general meetings may be ordinary and extra ordinary and comprise shareholders of all classes. Ordinary general meeting can be held only if the shareholders present or represented represent at least one-quarter of the shares of the voting shares. If this quorum requirement is not met, the meeting must be called a second time, and on that occasion no quorum is required. Resolution is passed at ordinary meeting by a simple majority of the voter held by the shareholders present or represented. Accordingly, a shareholder who abstains is disregarded.[52]

Any shareholder has the right to attend such meeting regardless of the number of shares he holds.[53]This is always true though there is contrary provision in the statutes of the company. He may also be represented by a third party whether shareholder or not.

Ordinary general meetings may take all decisions within the competence of the shareholders, except those which are required to be taken by an extra ordinary meeting. Decisions made by ordinary meeting mainly concern financial questions and matters concerned with the administration of the company. The most important kind of ordinary meeting is, of course the annual meeting, which must be held within four months after the end of each financial year.[54]

2.4.6.Extraordinary meetings' quorum and majority

Extraordinary meetings are subject to rigorous rules as to quorum and majority than ordinary meetings. At least half of the holders of all shares having voting rights of the company must be represented or presented at the meeting. If such quorum is not present the meeting must be called for the second or third time, and the quorum is reduced to one third, or one tenth respectively. Resolutions are passed at extra ordinary meetings by two-thirds majority of the votes held by shareholders present or represented.[55]

Resolutions to change the nationality of the company or increment of investment in the company require unanimous voting.[56] We can comment this provision as it does not the practical difficulty to get such unanimity. However we can at the same time take it as important provision to protect minority shareholders.

An extra ordinary meeting may alter any provision of the company statues provided that it does not increase the financial obligations of the shareholders, take away the basic rights of the shareholder, such as the right to transfer his shares of the right to vote at meetings or change.

2.4.7. Special meeting

Unlike meetings which may be attended by all shareholders of any class, special meetings may be attended by only the holders of a particular class of shares. For example, the holders of preference share, special meetings must be called to approve decisions of general meetings modifying the special rights attached to shares of the class in question.

[47]Supra note 35, Art. 398.
[48]Ibid, Art. 402
[49]Supra note 33.
[50] Supra note 5, P. 36.
[51]Supra note 35, Art. 399.
[52] Ibid, Art. 421
[53]Ibid, Art. 420.
[54] Ibid, Art. 418, 419.
[55] Ibid, Art. 425.
[56] Ibid, Art.425.

The decision of the general meeting to modify the rights of a class of share becomes effective only if the special meeting has given its approval.[57]

The rules as to quorum for special meeting and majority required to pass resolutions are the same as the rules governing extraordinary meeting. Therefore two-third majority is required to pass a resolution abstentions and blank ballots being disregarded. The quorum is said to be fulfilled if shareholders holding not less than half of all voting shares. It seems with the view to take practical situations into consideration that in a second meeting shareholders holding only one-third can satisfy the forum. The point here is that if shareholders in the first meeting fail to attend it will be practical and economic to reduce the quorum requirement.

2.5. Removal of directors

The law empowers the shareholders to remove a director by general meeting before the expiry of term of office. Even if there is no agenda regarding removal of directors[58]. However, a director so removed shall not be deprived of any compensation payable to him in respect of the termination of his appointment in the absence of good cause.[59] Directors can also be removed if shareholders representing one-fifth of the capital (20%) adopt a resolution to institute a proceeding.[60]The national bank can also remove directors, chief or senior executive officers for sufficient cause. Sufficient cause constitutes any administrative malpractice made by directors and officers with the view of the national bank.[61]

The Ethiopian commercial law and trade reform diagnosis suggests that shareholders should be enabled to remove a director without having to prove cause or provide special compensation, and that directors' remuneration must be approved by the shareholders and thus revising Article 354.[62]

2.6. Appointment of directors and auditors

The first directors may be appointed under the memorandum or articles of association. This appointment shall be submitted to a meeting of subscribers for confirmation. If such confirmation is not given, the meeting shall appoint other directors. Subsequent directors shall be appointed by a general meeting. Directors may not be appointed for more than three years. Unless otherwise provided in the memorandum or article of association directors are eligible for re-election.

In companies carrying out banking business the shareholders are not at liberty to appoint directors and chief or senior executive officers of their whim and wish in Ethiopia.[63] They are required to get the written approval of the national bank. We can see here that the regulatory body is there to protect the interests of other stakeholders.

Banking business in Ethiopia seems to be influenced by stakeholder theory than stock holder theory.

There should be a mechanism to the shareholders so that they may know about the qualification and other relevant personal details of the nominee. It is also necessary to prescribe the ways the shareholders can appoint a nominee. In short transparency is required in order that the shareholders can make informed vote.

As per article 368 of the commercial code, the general meeting shall elect one or more auditors and assistant auditors. Shareholders representing not less than 20% of the capital may appoint an auditor selected by them. According to art 372 the general meeting is to determine the remuneration to auditors. If the meeting fails to reach at consensus on the remuneration, the ministry of commerce and industry may fix the remuneration when any interested party applies to it.

Shareholders' rights to influence the corporation centre on certain fundamental issues such as the election of board members, or other means of influencing the composition of the board, amendments to the company's organic documents, approval of extraordinary transactions, and other basic issues as specified in company law and internal company statutes.[64]

Although board's executive contracts are not an appropriate subject for approval by the general meeting of shareholders, there should be a means by which they can express their views. Several countries have introduced an advisory vote which conveys the strength and tone of shareholder sentiment to the board.[65]

2.7. Right of withdrawal from the company

Shareholders who dissent from resolutions concerning any change in the objects or nature of the company or the transfer of the head office abroad may withdraw from the company and have their shares redeemed, at the average price on the stock exchange over the last six months. Where the shares are not quoted on the stock exchange, they shall be redeemed at a price proportionate to the company's assets as shown in the balance sheet for the last financial year.[66]

We can observe here that it is only when the listed circumstances are there that the shareholders can enjoy such rights. Therefore there seems no easy exit in Ethiopian company law. It seems better to further simplify the exit mechanism to any unsatisfied shareholder.

Such measure in other jurisdictions is known as compulsory bid. According to this rule, a shareholder who acquires control over a company is obliged to buy shares of minorities at the same price he paid for control.[67] In order to expedite these exit rights there is an urgent need to introduce stock markets. The absence of such institution may contribute to share illiquidity and individuals may decline from buying share. Fekadu Petros argue that in the absence of organized stock markets there can be no meaningful right of exit. We have seen in the first chapter that such easy exit mechanism plays important role to shape sharking managerial behavior in the diffused model of corporate governance.

2.8. Availability of ex-post redress for shareholders

A. Shareholder's right to initiate suits

One of the ways in which shareholders can enforce their rights is to be able to initiate legal and administrative proceedings against management and board members. Experience has shown that an important determinant of the degree to which shareholder rights are protected is whether effective methods exist to obtain redress for grievances at a reasonable cost and without excessive delay. The confidence of minority investors is enhanced when the legal system provides mechanisms for minority shareholders to bring lawsuits when they have reasonable grounds to believe that their rights have been violated.

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[57]Ibid, Art. 426.
[58]Ibid, Art. 397.
[59]Ibid, Art. 354.
[60] Ibid, Art. 365.
[61]Supra note 36, Art.
[62] Supra note 3, pp.23-24
[63] Supra note 36,Art. 14(2)
[64] Supra note 5, p. 32.
[65] ibid, p. 34.
[66] Supra note 35, Art. 463
[67] Supra note 1,. P. 29

The provision of such enforcement mechanisms is a key responsibility of legislators and regulators.[68]

There is some risk that a legal system, which enables any investor to challenge corporate activity in the courts, can become prone to excessive litigation. Thus, many legal systems have introduced provisions to protect management and board members against litigation abuse in the form of tests for the sufficiency of shareholder complaints, so-called safe harbors for management and board member actions (such as the business judgment rule) as well as safe harbors for the disclosure of information[69].

A balance must be kept between allowing investors to seek remedies for infringement of ownership rights and avoiding excessive litigation. Some countries have found that alternative adjudication procedures, such as administrative hearings or arbitration procedures organized by the securities regulators or other regulatory bodies are an efficient method for dispute settlement, at least at the first instance level.[70]

B. Derivative actions

There was a case against directors of Amanuel Stega Yenigid Sukoch Aksion Mahiber initiated by shareholders of the company in the Federal Supreme court Cassation division in 1999 under file no 23389. The applicants argued that the directors allocated the front rooms to themselves improperly. The respondents argued that they have no capacity to bring such suits. Even if we say they can initiate such suits the requirements under art 365 of the commercial code are not fulfilled. Under this article a resolution of general meeting has to be adopted by shareholders representing one fifth of the capital so as to institute a proceeding to enforce directors' liability. In addition to such resolution the shareholders need to wait for the company to institute the proceeding for three months. If the company fails to initiate the proceeding, the shareholders themselves may jointly institute the suit.[71]

The cassation court stated that the applicants can institute a suit if they can proof that their right is prejudiced. It argued that their suit is based on Article 367 of the commercial code and not by the provisions cited by the lower courts. Therefore the shareholders have ex-post redressing mechanisms if they can show that the directors acted to the prejudice of them.

The question here is whether the shareholders are empowered to initiate a suit against third parties representing the company if they believe that the company is prejudiced by the act of third parties. There seems no provision does exist to that effect. Art 365 is about directors' liability to the company and to the shareholders.

Shareholders derivative actions are law suits brought by individual company shareholders in the name of the corporation in which they hold stock. They arise when one or more stockholders believe managements are acting improperly, or are failing to take action to defend the company's rights. Here it is important to note that any benefit the suits are brought in the name of the company and any compensation won goes to the company, not to the share holders who initiated the suit.

3. Conclusion

Shareholders are normally owners of the corporation's assets and such assets are controlled by the management body is the cause for many of the problems dealt by corporate governance. Shareholders meeting as management organ can play considerable roles in corporate governance. The problem addressed by this article is therefore what necessary measures can further strengthen the shareholders controlling mechanisms on the corporation upon which they invested their capital. Even thought there are many theories concerning their roles in corporate democracy, none of them seem to win the battle. Whatever it may be there are however some areas of consensus.

Shareholders meetings can influence the corporation's governance by creating and amending statutory documents and other resolutions. The shareholders participation in the meeting and their voting properly handled and utilized can have positive impact in the corporation. Therefore the rules governing such meetings should be well designed in a way of enabling them play their part. It may include access of electronic voting, possibility of voting by mail, facilitating sufficient information disclosure mechanisms, adopting advisory voting and the rules necessary to such vote, facilitating easy exit mechanism to shareholders dissatisfied by majority holders, introduction of stock exchange market etc.

Existence of stock exchange market can increase shares liquidity and increase the stock owners' security as it enables them to exit easily if they feel discomfort by the management. It can also promote disclosure of information and transparency which is crucial to shareholders so that they can make informed decision in meetings or in any other way.

Moreover possibility of derivative suits by shareholders is also another mechanism that should be available to them to promote control. Rules as to derivative suits, proceedings representing the company against third party and the directors with the view to protect the company, should be adopted in Ethiopian commercial law. There are provisions that govern ex-post redressing mechanisms to shareholders against the directors. The law is silent about the possibility of instituting suits against third parties if the directors fail.

The minimum threshold to adopt a resolution to institute proceeding to enforce director's liability seems very high. Shareholders representing one-fifth of the capital should agree to adopt such resolution. It could be difficult to get such minimum requirement as it requires vote of shareholders holding 20% of the capital.

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