

Potential Reforms

Based on the key findings of the report, facilitating minority investor participation in the governance of privately-held companies and supporting minority investors to maintain the position they bargained for could be productive areas for improvement in protecting minority investors among APEC economies.

While opportunities for targeted and actionable reforms vary depending on the particular APEC economy, several common themes arise:



Facilitating minority investor participation: New technologies are allowing for virtual shareholder meetings. These should be legalized if not done so already. In addition, the use of cumulative voting to choose a board of directors increases opportunities for minority investors to appoint a member, ensuring minority investors are represented in corporate matters.



Protecting minority investor positions once acquired: Perhaps the policy in greatest need of review is one that would require a buyer of 50 percent of the shares of a privately held company to make a similar offer to the remaining shareholders. Only one of the 21 APEC economies requires such offers. If enacted into law, this tag-along right, which is often negotiated individually by savvy investors, would make it more likely for minority investors to receive the benefits of a buy-out of the company in which they have invested. Minority investors should also have a say in new investors coming in; or at least the right to buy shares before they are sold to outsiders.



Disclosure of related party transactions: Business deals between a company and a dominating shareholder occur often. While many of these transactions are fair and beneficial, they are sometimes used to channel resources out of a company at the expense of minority investors. These types of transactions should be disclosed to minority investors to give them the opportunity to challenge those that are abusive.

Even more important than any particular right are the real opportunities that minority investors have to enforce their rights, whether they are based on the law or individual negotiation. For minority investors in privately held companies, the **courts** are the main source of potential relief. Such cases, though, can often times be risky, especially where the judge is not familiar with corporate governance principles. While specialized courts could help, it is possible that the demand for cases is insufficient to justify establishing them.

One potential solution is to encourage companies to establish **arbitration mechanisms** to resolve disputes among investors and for APEC economies to clarify that their courts will respect such mechanisms if they are made clear in corporate charters or bylaws.

To download the full report:



PROTECTING MINORITY INVESTORS IN PRIVATELY HELD COMPANIES IN APEC

AT A GLANCE

PREPARED FOR:

APEC Economic Committee

PREPARED BY:

US-Support for Economic Growth in Asia
(US-SEGA)^P

APEC sets a high standard for protecting minority investors.

According to the World Bank's Doing Business Report, APEC economies, as a group, rank **42 out of 190** economies measured under its protecting minority investors index. This is a higher ranking than any other regional grouping aggregated by the World Bank, including the European Union, South Asia, and Latin America and the Caribbean. **However, protections for minority investors in privately held companies generally lag compared to those for investors in publicly traded companies.**

APEC demonstrates room for improvement in protections for minority investors in privately held companies.

The risks faced by minority investors in privately held companies can be complex and considerable. When unchecked by law or well-crafted shareholder agreements, a dishonest majority investor has substantial opportunities to shape company decisions for personal gain and to the detriment of minority shareholders. Further, minority investors in privately held companies cannot readily sell their shares in an organized exchange and cannot look to a market regulator, or even a private exchange, to establish and enforce corporate governance norms the way publicly traded firms can.

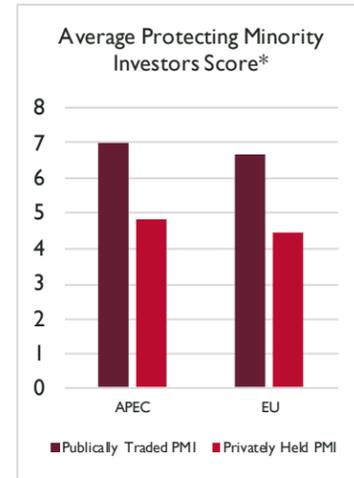
In this sense, **there is an opportunity for APEC economies to reduce the legal risk that equity investors face with regards for minority investors in privately-held companies**—i.e., typically small and medium-sized companies the shares of which are not traded on an organized securities exchange. Reducing such risk is likely to increase investment in smaller enterprises, offering a boost to a segment of firms that generate substantial income and employment across the region.

Since 2009, APEC Leaders committed to improving the business environment in the Asia-Pacific region through the **Ease of Doing Business (EoDB) Action Plan**. This action plan aimed to see a combined target of 25 percent improvement across key EoDB priority areas including: starting a business, getting credit, trading across borders, enforcing contracts, and dealing with permits. In 2018, APEC exceeded its target.

This report, undertaken under APEC's Economic Committee, aims to propose and build out Protecting Minority Investors as a new priority in the EoDB Action Plan's third iteration.

Methodology

This report focuses on the rules, regulations, and institutions that protect minority investors in privately held companies, and how these operate within APEC. The report first focuses on key elements of governance for privately held companies and the challenges faced by investors taking minority positions in privately



held companies. It also provides summary information on how APEC economies address some of these challenges. The report then discusses the various ways to mitigate the challenges facing minority investors: first by undertaking reforms suggested by Doing Business; by developing additional rules and safeguards; and finally by implementing potential practices that facilitate the use of courts and other mechanisms to enforce these rules and remedies.

Key Findings

The World Bank's Doing Business project annually tracks the extent to which economies have developed rules and institutions that protect investors. Despite strong protections for publicly traded companies, APEC economies demonstrate room for improvement in varying degrees when looking at policies for privately held companies. The figure below demonstrates where adoption of policies for protecting minority investors is still lacking, and areas where APEC can focus efforts moving forward.

Collecting accurate statistics on privately held companies in the region is far more difficult than doing so for their publicly traded counterparts. Though SMEs are not perfect proxies for privately held companies, a substantial portion of SMEs are indeed privately held companies with limited liability. Even when assuming a substantial portion of SMEs are sole proprietorships or single ownership corporations, this would still leave potentially hundreds of thousands of enterprises operating as multi-owner, privately held companies across the region.

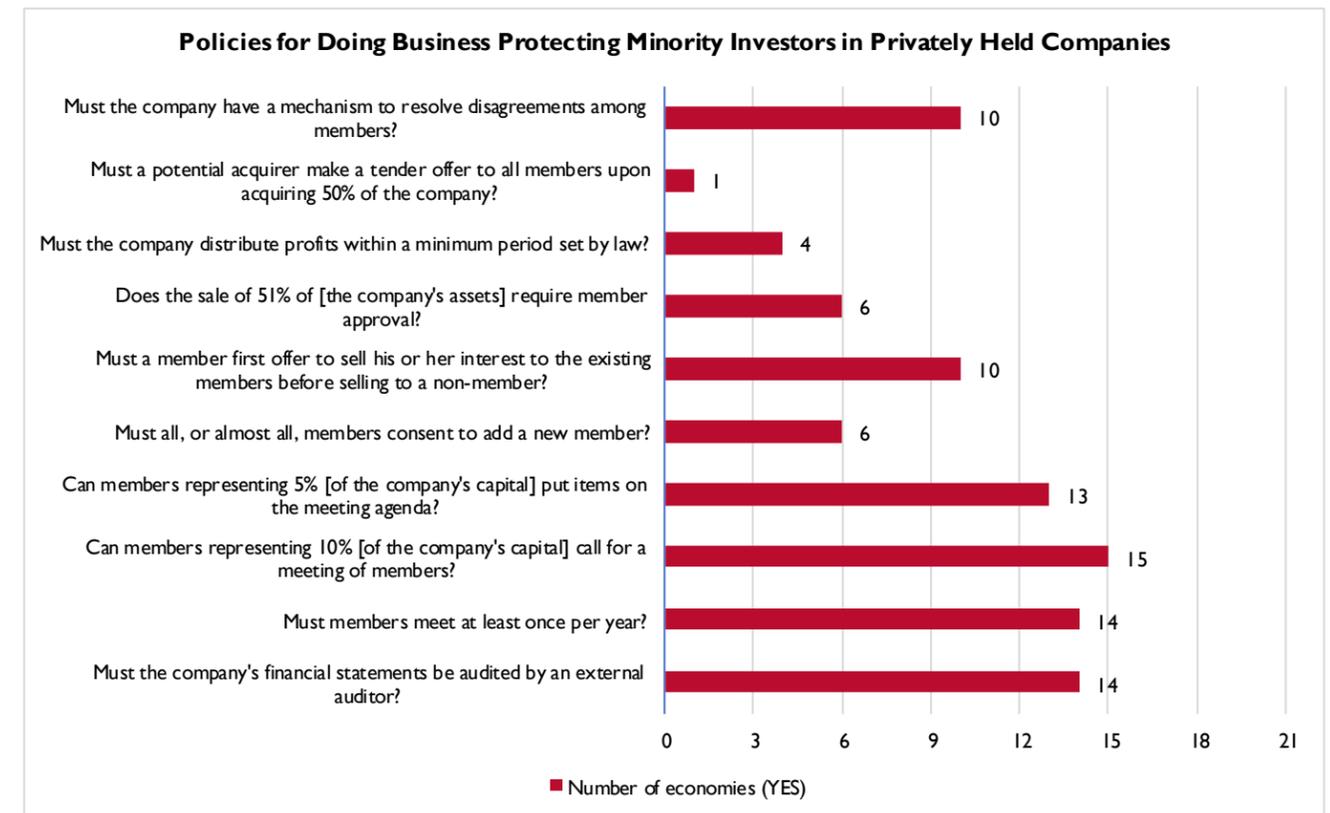


Figure 2.