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## The Organization of American States' Model Law on Simplified Corporations

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# THE ORGANIZATION OF AMERICAN STATES' MODEL LAW ON SIMPLIFIED CORPORATIONS

Francisco Reyes Villamizar\*

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#### ABSTRACT

*Colombian Law 1258 of 2008 introduced the Simplified Corporation (Sociedad por Acciones Simplificada or SAS). This type of business entity included modern corporate law features such as simplified incorporation proceedings, full-fledged limited liability for its shareholders, and broad freedom of contract for the definition of housekeeping and governance rules. It also reduced old-fashioned prohibitions pertaining to shareholders and managers activities and reduced transaction costs. The SAS's "opt-in" approach also has allowed for private parties to draft the most suitable agreements. The enabling provisions of Law 1258 have been the starting point for the preparation of at least three Model Law proposals presented before the Organization of American States (OAS), the United Nations Commission for International Trade Law (UNCITRAL), and the Pacific Alliance.*

*Discussions on these draft legislative models have been underway over the last few years at different bodies within these multinational organizations. Although some progress has been made in recognizing the importance of providing some degree of harmonization in the field of closely held business enterprises, particularly in developing jurisdictions, there are still significant obstacles that need to be surpassed before such model law is adopted. In June, 2017 the OAS General Assembly recommended to the Organization's member States to adopt the Interamerican Model Law on Simplified Corporations. It is the first successful attempt for the international harmonization on the rules concerning business corporations.*

**Keywords:** corporate law, model law, simplified corporations, harmonization, Columbian SAS, Organization of American States

## I. INTRODUCTION: A MODEL LAW ON SIMPLIFIED CORPORATIONS

On June 20, 2017, the General Assembly of the Organization of American States (OAS) adopted a resolution<sup>1</sup> in which it requested the Inter-American Juridical Committee and its Technical Secretariat to give the broadest possible publicity to the Model Law on Simplified Corporations. In the same resolution, the General Assembly requested the General Secretariat to provide the OAS Member States all the necessary cooperation and support if they decided to adopt the Model Law or any parts thereof. The General Assembly's decision represents a significant step towards the harmonization of company law in the Americas, since it is the first instrument ever produced in this legal area.<sup>2</sup>

This paper discusses the OAS Model Law on Simplified Corporations<sup>3</sup> (hereinafter also referred to as the "Model Law"), and analyzes harmonization of laws concerning closely held entities, especially in emerging jurisdictions. This paper also contains an analysis concerning some of the current legislative approaches to corporate law existing in emerging jurisdictions, and summarizes certain difficulties that entrepreneurs encounter when confronted with legal formalism. It also describes the scope of the Model Law and the legislation upon which it was based, i.e., the Colombian Law on Simplified Corporations (hereinafter also referred to as "Colombian

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1. See Model Law on the Simplified Corporation, Resolution AG/RES.2906 (XLVII-O/17), adopted at the first plenary session held on June 20, 2017. For the Model Act on the Simplified Stock Corporation, see <https://perma.cc/X92E-DDM9> [hereinafter Model Law].

2. The resolution was adopted by unanimous consent at the General Assembly with the exception of Venezuela.

3. During its March 2011 regular session, the Inter-American Juridical Committee approved the Model Law on Simplified Corporations. See *Project for a Model Act on Simplified Stock Corporation*, CJI Res. 188 (LXXX-O/12), CJI/doc.380/11 (Mar. 9, 2012) [hereinafter OAS Resolution 188]; See also *Draft OAS Model Law on the Simplified Stock Corporation (SAS) considered at Annual Meeting of ASORLAC*, OAS NEWSLETTER (Oct. 2014), at <https://perma.cc/6EVA-ASQ4>. On various occasions, the Model Law was presented before the Committee on Juridical and Political Affairs. This body remanded the initiative to the Permanent Council which, on its meeting of June 14, 2017 adopted the resolution concerning the Model Law, which was eventually sent to the OAS; See OAS G.A. Res. 2609, AG/doc.5579/17, at <https://perma.cc/2MAT-NLNR>.

SAS”).<sup>4</sup> In this vein, the empirical data distilled from the Colombian experience illustrates the appropriateness of most solutions proposed in the Model Law.

Following this brief introduction, section II discusses the objective behind the enactment of the Model Law, and the current problems affecting the Latin American legislative agenda. The core idea is that the adoption of the Model Law will help broaden the formal economy and foster economic growth and welfare for the population. In fact, it is well known that formalization is a crucial factor without which businesses find it hard to have access to credit from financial institutions; the state cannot collect revenues derived from taxes, and workers are deprived from social security benefits. It is argued that introducing the forward-looking rules contained in the Model Law can correct most corporate law deficiencies in the region and could produce the desired economic results. Section III contains a summary of the main contents of the Model Law, as well as an explanation as to how these provisions can improve current corporate law in the region. Section IV contains empirical data on the Colombian experience concerning the *Simplified Corporation* (SAS by its Spanish acronym) over nearly a decade. The relevance of the Colombian SAS is emphasized given its significant influence in the preparation of the Model Law. The collection of empirical data provides compelling arguments in favor of the Model Law’s adoption. Section V provides an analysis of the Colombian Specialized Corporate Law Court. This section is intended to underscore the fact that, in order for substantive legal transplants in the corporate sphere to be effective, they must be accompanied by reforms aimed at strengthening the institutional infrastructure. Lastly, section VI presents a few relevant conclusions.

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4. Colombian Law on Simplified Corporations introduced by Law no. 1258, Dec. 5, 2008, DIARIO OFICIAL [D.O.].

## II. WHY A MODEL LAW ON SIMPLIFIED CORPORATIONS?

The Model Law is aimed at reducing transaction costs in starting, carrying out, and closing any given business venture, irrespective of its dimensions or business activity. It is argued that reducing transaction costs for business fosters economic growth and trade, and may incentivize formal economic activity in emerging economies. World Bank researchers have found that “informality is not single-caused but results from the combination of poor public services, a burdensome regulatory regime, and weak monitoring and enforcement capacity by the state.”<sup>5</sup> The initiative is thus intended to counter the final two characteristics of informality: a burdensome regulatory regime and weak enforcement capacity by the state. It is expected that reducing informality by setting up an enabling environment for business, will ultimately enhance economic development and provide welfare for the people of a given jurisdiction.<sup>6</sup>

The Model Law initiative is also intended to fulfill additional useful purposes. First, regional trade may be increased by a process that involves simplifying the legal formalities required for undertaking entrepreneurial activity. Second, at the local level, defining a less onerous threshold for businesspersons setting up micro, small, and medium enterprises (MSMEs) to enter the formal economy may be achieved by simplifying the incorporation process. Finally, there is also an academic purpose in the Model Law initiative. Despite the importance of comparative company law as an academic discipline, before the OAS Model Law, there had not been any comprehensive initiatives geared towards the creation of a harmonizing instrument in this area of law. In 2006, comparative law professor Klaus J. Hopt

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5. Norman Loayza, Luis Servén & Naotaka Sugawara, *Informality in Latin America and the Caribbean* (World Bank Policy Research Working Paper Series, Paper No. 4888, Apr. 20, 2016), available at <https://perma.cc/QJ3Z-6QXE>.

6. According to Hansman and Kraakman, the general goal of corporate law is to advance aggregate welfare of constituencies affected by the activities of an enterprise. The Model Law intends to further said goal. See REINER KRAAKMAN ET AL., *THE ANATOMY OF CORPORATE LAW—A COMPARATIVE AND FUNCTIONAL APPROACH* ch. 1 (3d ed., Oxford U. Press 2017). The goals advanced by the Model Law are in line with contemporary policies that give preference to business forms referred to as “uncorporations.” See LARRY RIBSTEIN, *THE RISE OF THE UNINCORPORATION* ch. 1 (Oxford U. Press 2009).

complained about the absence of such a project: “In view of the golden age of the elaboration of common principles of law such as the UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law, it is astonishing that similarly successful work has not yet been undertaken in the area of company law.”<sup>7</sup> The initiative also intends to serve as a stepping-stone to fill this gap in private international law.<sup>8</sup>

The initiative assumes that harmonization of the company law framework within Latin America may be achieved.<sup>9</sup> This endeavor involves two distinct processes: (i) reaching a common understanding between different, albeit related, legal systems; and (ii) facilitating the mutual recognition of corporations doing business in a designated region. In this context, achieving a common understanding refers to bridging the different legal languages within various jurisdictions. Arguably, reaching a set of homogenous legal terms will promote economic integration by facilitating the interaction between entrepreneurs (and their advisors).<sup>10</sup> Achieving a mutual

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7. Klaus J. Hopt, *Comparative Company Law*, in THE OXFORD HANDBOOK OF COMPARATIVE LAW 1172 (Reimann & Zimmermann eds., Oxford U. Press 2008).

8. It is relevant to underscore the efforts of the Organization for the Business Law Harmonization in Africa (*Organisation pour l'Harmonisation en Afrique du Droit des Affaires*) (OAHADA). The treaty that gave rise to this organization was executed in Port Louis, on October 17, 1993, and later revised in Quebec, on October 17, 2008. This organization has passed a uniform act on corporations, which regulates, *inter alia*, the relationships among shareholders, the integration of corporate organs, the management of the corporation, the access to capital, and the transfers of shares of stock. The Uniform Act is applicable to all signatory states of the Harmonization Treaty. There are 17 OAHADA states: Benin, Burkina Faso, Cameroon, Central African Republic, Chad, Comoros, Côte d'Ivoire, Democratic Republic of Congo, Equatorial Guinea, Gabon, Guinea, Guinea-Bissau, Mali, Niger, Republic of the Congo, Senegal, and Togo.

9. Since Model Laws are legislative instruments that are not vested with any coercive powers, it is up to each of the member state governments to adopt such rules altogether or to use them as a prototypical structure that can be partially imitated. Thus, one of the main benefits of the Model Law is to offer legislators of all OAS member states broad parameters on the topic, so that each legislature can find inspiration for the enactment of its own corporate laws, and if the case may be, to take advantage of the model provisions to harmonize its legislation by incorporating the above-quoted best practices.

10. The experience of the EU law harmonization is useful. It has been argued by the European Commission that “disparate national law rules may lead to higher transaction costs, especially information and possible litigation costs for enterprises in general and SMEs and consumers in particular.” See E.C. O.J. 2001,

recognition of corporations relates to the process of hosting a foreign entity in a local jurisdiction without requiring compliance with cumbersome and costly formalities in the receiving country.<sup>11</sup> The effective mutual recognition of foreign enterprises is also intended to promote cross-border entrepreneurial activity and to reduce transaction costs involved in operating in new markets.

At the local level, it is well-known that millions of MSMEs currently face significant formalistic barriers preventing them from entering the formal economy.<sup>12</sup> Transaction costs are here evident in light of the cumbersome proceedings required to undertake the process of incorporation. In the Latin American region, the informal economy is prevalent and micro and small entrepreneurs frequently find that the benefits of operating formally are outweighed by the

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*Communication from the Commission to the Council and the European Parliament on European Contract Law* (2001/C 255/01) 5, no. 31, at <https://perma.cc/H4A8-HJGF>. Facilitated interaction between businesspersons will entail a reduction of costs and will also facilitate economic integration within the region. FRANCISCO REYES, II LATIN AMERICAN COMPANY LAW—A NEW POLICY AGENDA: RESHAPING THE CLOSELY HELD LANDSCAPE 67 (Carolina Acad. Press 2013):

Harmonization in the field of company law could be a sensible step in the context of the process of integration, particularly taking into consideration the fact that several countries throughout the region have either entered into or are in the process of negotiating free trade agreements with the United States.

11. The concept of mutual recognition is explained by Nicolaidis & Shaffer: Mutual recognition regimes set the conditions governing the recognition of the validity of foreign laws, regulations, standards, and certification procedures among states in order to assure host country regulatory officials and citizens that their application within their borders is “compatible” with their own, and that incoming products and services are safe. These conditions involve different types of obligations for *home states*, who benefit from conditional recognition of the laws and regulations applicable to products, persons, firms and services, and *host states*, who forego the application of their own rules to products, persons, firms and services, provided that the agreed conditions are met.

Kalypto Nicolaidis & Gregory Shaffer, *Transnational Mutual Recognition Regimes: Governance without Global Government*, 68 LAW & COMTEMP. PROBS. 264 (2004).

12. Studies on informality in Latin America show the link between highly informal economies and formalistic barriers to achieve an organized business activity: “Informality is sometimes the result of agents ‘exiting’ the formal sector as consequence of cost-benefit considerations; other times, it is the outcome of agents being ‘excluded’ from formality as this becomes restrictive and the economy segmented.” See Loayza, Servén & Sugawara, *supra* note 5, at 2.

high costs involved in such operation.<sup>13</sup> The existence of an informal economy also results in the loss of opportunities for foreign investment, which is crucial for less developed economies.<sup>14</sup> Thus, such informality also impacts the collection of taxes which, in turn, hinders the availability of funds for revenue distribution.<sup>15</sup>

Business informality in several countries of Latin America reaches high figures that can be even above 50 percent. According to Professor David Stewart, a study shows that:

[I]n our hemisphere, both big and small economies depend upon informally-created micro and small companies (“MiPymes”) for much of their employment. In El Salvador, MiPymes accounted for 99.6% of all of businesses in 2005, and 90.52% of these were microenterprises located in urban areas and especially in the capital city of San Salvador. Most Salvadoran micro-businesses are conducted by a single individual or with the assistance of one or two additional employees. In Brazil, according to a report from the *Serviço Brasileiro de Apoio às Micro e Pequenas Empresas* (Brazilian Service for the Support of Micro and Small Businesses), the number of microenterprises grew 9.1% from 1997 to 2003, from 9,477,973 to 10,335,962, employing over 13 million people. In Mexico, 99% of all Mexican businesses fall under the rubric of “micro,” “small” or “medium-sized” enterprises, employing approximately 60% of the population,

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13. The Organisation for Economic Co-operation and Development (OECD) presents the link between informality and, among others, regulatory restraints: “Informality and gender gaps remain high, and social mobility low.” OECD, *OECD Economic Surveys: Colombia 2017* (Paris, May 2017), <https://perma.cc/7GYD-J3S9>.

14. World Bank researchers have evidenced the correlation between the informal sector and low levels of investment: “[T]he informal sector contributes to an inimical investment climate for formal firms, particularly foreign investors. Further, the informal sector in general and large informal firms in particular are responsible for a substantial loss of fiscal revenues and narrowing of the tax base.” Nancy Benjamin, Kathleen Beegle, Francesca Recanatini, & Massimiliano Santini, *Informal Economy and the World Bank* (World Bank Policy Research Working Paper Series, Paper No. 6888, Apr. 20, 2016), available at <https://perma.cc/57FB-3QSG>.

15. For the purposes of this paper, an informal enterprise is that in which no registration process, or other specific formalities required by each jurisdiction, has been undertaken. See Abby Margolis, *The Value of Informal Enterprise*, STANFORD SOCIAL INNOVATION REVIEW, Nov. 1, 2012, <https://perma.cc/TM4X-QKZD>.

and MiPymes are responsible for more than 20% of Mexico's gross domestic product.<sup>16</sup>

To further illustrate the problem of informality of MSMEs, it is suitable to refer to the data collected by the World Bank in 2015<sup>17</sup>:

- In the developing world, there are between 365 million and 445 million MSMEs.
- Of that number only 25–30 million are formal Small and Medium Enterprises (SMEs) and, only, between 55–70 million are formal Micro Enterprises.
- 285 out of 345 million MSMEs, over 70% are considered informal and consequently, lack access to credit.

In contrast with the data above, four out of every five jobs in emerging economies are created by MSMEs, providing over 33% of the national income in these jurisdictions.<sup>18</sup> These data reveal the importance of MSMEs for emerging economies, as well as the existing potential for developing a strong formal economy.

As a result of informality, these MSMEs, which make up the bulk of the productive capacity, lack access to credit. The following image contains a map of the World showing the credit gap between informal and formal firms:

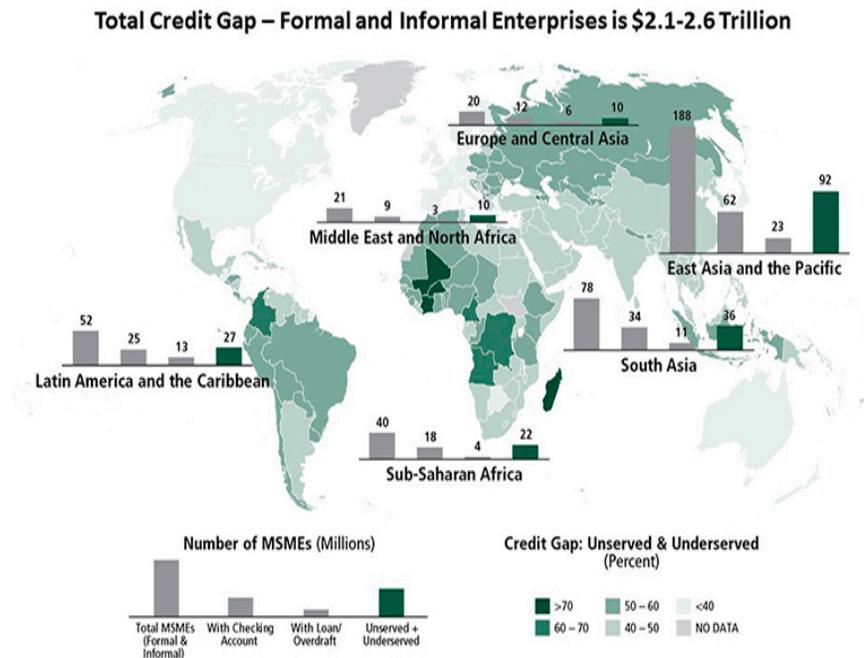
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16. See David Stewart, *Recommendations on the Proposed Model Act on the Simplified Stock Corporation*, Annual Report of the Inter-American Juridical Committee 50 (2012) (quoting a study prepared by Boris Kozolchyk & Cristina Castaneda). See also OAS Resolution 188, *supra* note 3.

17. Simon Bell & Ghada Teima, *Small and Medium Enterprises (SMEs) Finance*, THE WORLD BANK, Sep. 1, 2015.

18. See Margolis, *supra* note 15. See also, e.g., Donald C. Clarke, "Nothing but Wind"? *The Past and Future of Comparative Corporate Governance*, 59 AM. J. COMP. L. 104 (2010):

Non-public-corporation business organizations (NPCBOs) play a major role not just in advanced industrialized economies, but even more in the transition and emerging market economies that have become increasingly important. They are major sources of employment, and are an essential stage in the life cycle of the large, successful public corporation. To focus on public corporations without understanding how NPCBOs operate, then, is to overlook a major part of the global economic landscape.

**Figure 1.** Total Credit Gap Map<sup>19</sup>

The implications of the lack of access to credit for MSMEs are noteworthy. Firms that cannot access legal sources of finance have limited growth opportunities and therefore cannot contribute to the economy in a significant way.<sup>20</sup> Formalization of MSMEs is needed in order to provide capital-raising opportunities for large sectors of the economy.

In furtherance of the objectives set out above, the Model Law initiative is aimed at creating the appropriate incentives in order for informal firms to migrate into the formal economy. This will be done mainly by introducing less burdensome incorporation procedures and reducing transaction costs in general throughout the life cycle of the firm. The underlying concept is straightforward: firms should be able to comply with a simplified registration process, facilitating incorporation, and ensuring compliance with basic regula-

19. See Margolis, *supra* note 15.

20. See Bell & Teima, *supra* note 17.

tions. As the World Bank has stated: “Studies have shown that removing excessive bureaucratic formalities in the startup process has numerous benefits for both economies and entrepreneurs. Some of these gains include higher levels of firm formalization, economic growth and greater profits.”<sup>21</sup> For many decades it has been compellingly argued that migration into the formal system will produce several benefits including the following: higher tax revenues, better regulation, social security protection and labor formalization, higher levels of transparency and disclosure, better access to credit and government services, and higher levels of investment.<sup>22</sup> Other positive consequences for fully complying firms are benefitting from limited liability and asset partitioning, among others.<sup>23</sup>

#### A. Focus on Latin America

The Model Law has been designed with a focus on Latin America.<sup>24</sup> There are two reasons for this regional approach. First, the Colombian experience with the recent introduction of the SAS provides a compelling body of statistics and facts (discussed in depth below), which can serve as a benchmark for the adoption of this model in other similar jurisdictions. Second, the Latin American scenario offers useful features given the size of the economies in this geographic area, as well as the transitional nature of their economies.

In line with the initiative’s regional focus, as stated by Jeannette M.E. Tramhel, the OAS Model Law is grounded upon the Colombian legislation:

[B]oth the Colombian Law and the SAS Model Law on which it is based contain the key elements that are essential

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21. See World Bank Group, *Doing Business 2017: Equal Opportunity for All*, doc. 14 (Washington, D.C., 2017), at <https://perma.cc/9ZQ8-TTBC>.

22. See HERNANDO DE SOTO, *EL OTRO SENDERO—LA REVOLUCIÓN INFORMAL* ch. 3, 220 (7th ed., La Oveja Negra 1987).

23. For an insightful discussion into the characteristics of the firm and its many benefits, see KRAAKMAN ET AL., *supra* note 6.

24. Latin America consists of 22 countries, with seven official languages, a total population of about 605 million people, and a surface of roughly 22,222,000 km<sup>2</sup>. See *South America: Physical Geography*, NATIONAL GEOGRAPHIC SOCIETY, <https://perma.cc/KZ8K-PER4>.

to simplified incorporation . . . . These elements could be considered to comprise ‘global best practices’ as most have been identified as key by various entities, including the World Bank, the United Nations Commission on International Trade Law (‘UNCITRAL’) and the United Nations Conference on Trade and Development (‘UNCTAD’), among others.<sup>25</sup>

A second feature of the Model Law initiative relates to excluding listed companies from its scope. In this way, the accent has been placed on closely held entities. It is a well-known fact that most companies in Latin American are family owned and trade outside of stock exchanges.<sup>26</sup> Recently, the Organisation for Economic Cooperation and Development (OECD) published its Corporate Governance Factbook for 2017, noting the highly concentrated ownership

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25. Jeannette M.E. Tramhel, *The Simplified Corporation: A New Structure for Doing Business in the Americas?*, 24 AGENDA INTERNACIONAL 144-145 (2017). Likewise, Professor David Stewart recognizes the significant influence that the Colombian simplified corporations law had on the OAS initiative:

Under the Colombian approach, the SAS can be formed by one or more shareholders and can be incorporated by a relatively simple private or electronic document (as opposed to an expensive notarial deed of incorporation). The cost is minimal. The act of incorporation provides limited liability to its shareholders (except when the corporate veil is used to perpetrate a fraud or abuse the corporate form). It also provides protection to third party victims of the abusive or fraudulent use of the *ultra vires* doctrine by corporate officials. It enables the founders to choose an unlimited duration for the incorporation, and replaces the costly and ineffective formality of mandatory internal comptrollers (*comisarios*) with a more effective and less expensive supervision of external but fully qualified auditors. It also provides flexibility to corporate capital, greater contractual freedom, and increased access to capital.

*See* Stewart, *supra* note 16, at 50. *See also*, Jorge Oviedo Albán, *La sociedad por acciones simplificada en el derecho colombiano*, in LA TIPOLOGÍA DE LAS SOCIEDADES MERCANTILES—ENTRE TRADICIÓN Y REFORMA 174 (Grupo Editorial Ibañez 2017) [hereinafter SOCIEDADES MERCANTILES]: “It is noteworthy that Law 1258 [of 2008] on simplified corporations has formed the basis for the Model Law enacted by the Organization of American States’ Inter-American Juridical Committee, in its 80th Session Period . . . .”

26. The empirical analysis of the Brazilian corporate market by Érica Gorga evidences the characteristics generally seen throughout the region:

The study of Brazilian economic reality has shown that the model proposed by Berle and Means may not serve as a basis for the analysis of Brazilian corporate law. In fact, the Brazilian corporate reality did not follow the same development trend that the American corporations did. In Brazil, as a general rule, there is no degree of disjunction between property and control, which supports the theory of Berle and Means.

ÉRICA GORGA, DIREITO SOCIETÁRIO ATUAL 129 (Elsevier 2013).

structure of listed companies in several Latin American jurisdictions.

**Table 1.** Ownership Structures at Company Level<sup>27</sup>

Jurisdiction	Ownership structure
Brazil	A large majority of listed firms are controlled by a single shareholder, foreign firms or via pyramidal structures involving corporate groups. A survey of 201 listed firms (85% market cap) found that over 70% of the firms had either family or shared ownership control (OECD, 2011a).
Chile	As of 2002, some 50 major conglomerates had ownership control of more than 70% of non-financial listed companies. The median controller holds 67% of shares, while less than 1% of firms are widely held when applying the threshold of 10% of ownership (OECD, 2011b).
Colombia	Colombian companies have a highly concentrated ownership structure. Among the largest listed companies, the controlling shareholders retain more than two thirds of total shares.
Mexico	Listed companies are characterised by a high degree of concentration. Company groups are the common feature in the market, and many of them are owned by family groups.

Noting the trend above, it is useful to establish the relative size of the securities markets in the region in terms of number of listed companies. For example, Brazil, the region's largest economy also has the greatest number of listed companies. In 2010, there were 400 corporations listed in the Sao Paulo Stock Exchange (the BOVESPA).<sup>28</sup> In contrast, for the same period the United States had approximately 5,000 listed companies in the U.S. stock markets.<sup>29</sup>

The focus on non-listed companies is also a characteristic of the Colombian law of 2008. Pursuant to Law 1258 of that year, the SAS is not intended to go public. The underlying rationale here is that the level of flexibility of these provisions is incompatible with the shareholder protection that is needed concerning listed corporations. In accordance with Article 4 of the aforementioned law, the shares of stock and any other securities issued by a simplified corporation

27. OECD, *OECD Corporate Governance Factbook 2017*, 12 *et seq.* (2017), <https://perma.cc/248B-SEA3>.

28. See Pierre Habbard, Hans-Böckler-Foundation, *Corporate Governance in Brazil - An International Trade Union Perspective* (Paris, Apr. 2010), <https://perma.cc/T85D-XSBS>.

29. See Board of Governors of the Federal Reserve System, 2010 Bogle Financial Markets Research Center, <https://perma.cc/KVN7-YR3X>.

shall not be listed in the National Registry of Securities and Issuers, nor traded in any stock exchange.

Inspired by the Anglo-American approach to securities regulation, as well as certain European models such as the German *Neuer Markt*, there have been attempts to broaden some Latin American securities markets, but this has had limited success.<sup>30</sup> The approach adopted in the Model Law is different. One of the main objectives of the initiative is to offer MSMEs a simplified framework to facilitate low cost access to the formal sector, and thus to bank financing. This proposal is coherent with the corporate structure prevailing in Latin America where the bulk of the economic building capacity is associated with MSMEs, instead of firms large enough to trade their stocks on the securities markets. This orientation is not intended to suggest that the introduction of high corporate governance standards is to be ignored. However, efforts should now be directed towards introducing and consolidating corporate governance standards specifically tailored to the characteristics of the Latin American markets.

The approach of the Model Law also responds to the need for a specific set of provisions directed at the establishment and operation of closely held entities. General corporate law in Latin America has responded to the codification models adopted in the region, which sometimes fail to provide for regulation aimed at the close corporation. American scholars have acknowledged the need to introduce these types of statutes:

Corporate statutes try to fit corporations closely held by a

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30. José Miguel Mendoza, *The Controlling Shareholder as Reputational Intermediary* (Oxford Centre for Corporate Reputation Working Paper Series, Paper No. 302, Mar. 5, 2012), <https://perma.cc/745X-GGLC>:

More than a decade on, the results of these experiments in legal reform have been disappointing. Convergence around formal rules of investor protection has not contributed significantly to the growth of stock markets in emerging countries. Empirical tests in fact show that these efforts were mostly futile and in many cases counterproductive.

For the discussion regarding the adoption of more European models, see Bruno Salama & Viviane Muller, *Legal Protection of Minority Shareholders of Listed Corporations in Brazil: Brief History, Legal Structure and Empirical Evidence*, 4 J. CIV. L. STUD. (2011), available at <https://perma.cc/5EYM-XF9T>.

few shareholders into the same legal clothes worn by publicly-held corporations. But it's a poor fit. The shareholders of a close corporation are likely to think of themselves as partners who incorporated their business to obtain limited liability or sometimes for tax reasons. They often find that the corporate rules of centralized management and majority control are at odds with their expectations of decentralized equality. They may wonder why they can't simply manage the business as they agree.<sup>31</sup>

*B. Problems with the Legislative Agenda in the Latin American Region*

Throughout Latin America, it is hard to find investment vehicles that can serve the business community with legal structures endowed with enough flexibility to respond adequately to the demands of trade in the modern world. The lack of modern regulations aimed at facilitating the incorporation and operation of business entities can become a meaningful obstacle for job creation and access to credit and, more generally, to economic development. Many of the corporate structures present in Latin American and Caribbean countries date back to 19th century regulations characterized by formalism and several restrictions to private ordering.

The Model Law on Simplified Corporations contains basic provisions that would allow business entities of varying dimensions to incorporate and operate in conditions that are appropriate to their economic needs. Despite the fact that the simplified corporation is particularly suitable for MSMEs, it is also true that it can be used to structure businesses of a larger dimension.

Following is a discussion of some of the prevailing characteristics of Latin American corporate law that constitute a hindrance to the formalization of new business entities in the region.<sup>32</sup> Thus, by taking into consideration the problems with the legal regime, the

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31. ALAN PALMITER & FRANK PARTNOY, CORPORATIONS: A CONTEMPORARY APPROACH 1001 (West 2010).

32. For a more comprehensive analysis, see REYES, *supra* note 10. Although this paper is centered in Latin America's legislative agenda, it is noteworthy that some of the findings are not exclusive of this geographic area, and therefore may also be applicable to different emerging nations such as those located in parts of Asia and Africa.

Model Law is intended to provide tailor-made solutions that are suited to the specific needs of Latin American businesspersons.<sup>33</sup> As recently noted by Jeannette M.E. Tramhel, commenting on the problems with Latin American corporate law: “[A]s a result of these aspects of company law, which run counter to global best practices described above, many Latin American businesses are significantly restricted and operate at a competitive disadvantage. Although this situation affects all business, the consequences are particularly severe for MSMEs.”<sup>34</sup>

### *1. Entry Barriers*

The first issue is the excessive and cumbersome set of formalities that businesspeople have to endure in order to incorporate in the region. Some legal scholars believe that excessive formalism in Latin America is derived from Spanish and Portuguese colonial heritage, which has been embedded in the region’s legal DNA.<sup>35</sup>

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33. As noted above, the Model Law is in line with the Colombian legal reform of the SAS. The initial diagnosis and the objectives of both pieces of legislation are very similar:

The starting point for the Simplified Corporation’s original proposal was the idea of facilitating the formalization of business entities and updating the legal system in order to introduce forward-looking approaches to Corporate Law. For that purpose, a thorough critical revision of the previous Company Law framework was required. This analysis was made under a functional Comparative Law methodology along with the application of relevant notions of Economic Analysis of Law. As expected, the results of such evaluation revealed the inadequacy of most Company Law provisions in place and the need to carry out an overhaul of both the legal and the institutional frameworks.

Francisco Reyes, *The Colombian Simplified Corporation An Empirical Analysis of a Success Story in Corporate Law Reform*, 4 PENN. ST. J.L. & INT’L AFF. 392, 396 (2015), available at <https://perma.cc/7B7J-2Q76>.

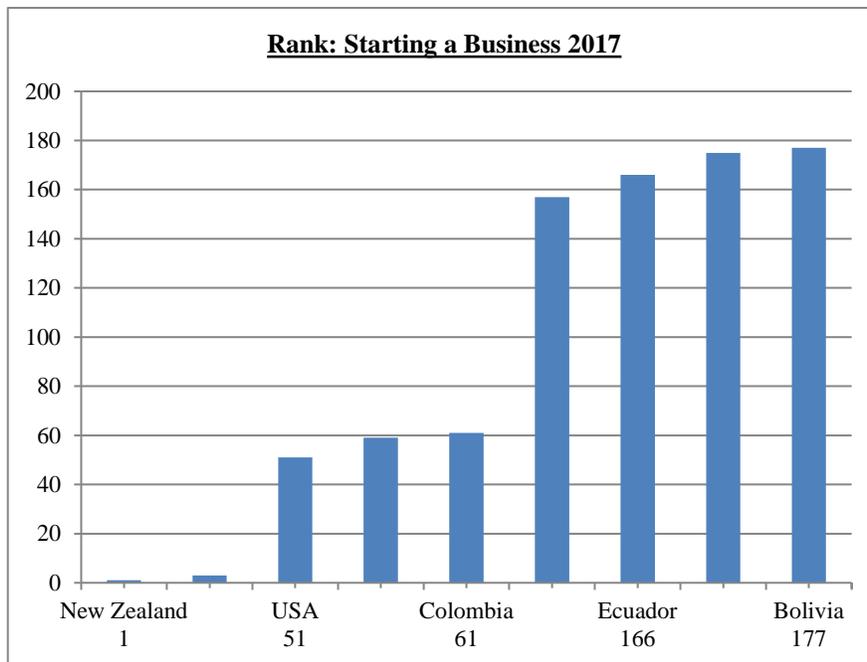
34. See Tramhel, *supra*, note 25, at 9.

35. This legalistic trait is masterfully explained by Keith Rosenn in his analysis of Brazilian legal culture:

Closely related to legalism is the exaggerated concern with legal formalities. Every nation has some formalistic behavior, but Brazilian concern with authenticity and verification is both impressive and oppressive. Legally permitting a friend to drive one’s car requires written, notarized authorization. In many situations the signature of the notary must itself be verified. Foreigners may be validly divorced abroad, but before Brazilian officials will accord the foreign decree any validity, the document must be translated by the Foreign Office and homologated by the Supreme Federal Tribunal . . . . The presumption appears to be that every

The Doing Business Index published by the World Bank is helpful in identifying the problems created by excessive formalism. One of the areas measured by the Index is the ease (or difficulty) of starting a business. Figure 2 below compares the number of days required to incorporate (or start a business) in several jurisdictions. Most Latin American jurisdictions are badly ranked.

**Figure 2.** Selected Ranking: Expedience of Incorporation Proceedings<sup>36</sup>



Upon reviewing the best practices of highly ranked jurisdictions in the Doing Business Index, it is noticeable that countries with the best performance offer entrepreneurs a set of enabling rules that facilitate incorporation. Ease of starting a business is founded upon

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citizen is lying unless he produces written, documentary proof that he is telling the truth.

Keith Rosenn, *The Jeito: Brazil's Institutional Bypass of the Formal Legal System and its Developmental Implications*, 19 AM. J. COMP. L. 514, 530 (1971).

36. Data taken from World Bank website; see World Bank Group, *supra* note 21.

online procedures, a limited number of forms that have to be filled in order to accomplish the process, and the absence of notary publics or registrars with costly and lengthy formalities. In New Zealand, for example, the entire process can be completed by applying for registration on the Companies Office's website,<sup>37</sup> and it takes only a few hours to complete. The World Bank recommends the implementation of the so-called "one stop shop strategy" by which all proceedings related to incorporation can be accomplished before a single window, either physical or virtual. In this manner, a single governmental office is entrusted with processing not only the business registration but also the tax ID, social security, business licenses, etc. Within developing jurisdictions, the case of Kenya is a good example of improvement made by providing an efficient business registration system.<sup>38</sup>

At the other end of the spectrum, the World Bank argues that Brazil incorporation takes an overwhelming 101 days.<sup>39</sup> This is the result of a highly bureaucratic procedure. The general rule in Latin American countries is that incorporation requires that the applicant personally appear before the respective governmental entity (tax, social security, pension and severance funds, notary public, mercantile registry, foreign direct investment registration, environmental permits, business license, etc.), fill out long forms,

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37. See *Companies Register*, NEW ZEALAND COMPANIES OFFICE, at <https://perma.cc/V2LX-MMED>. The first step is to log on through the setting up of a user account on the designated website. Afterwards, the applicant must reserve the corporate name, complete the relevant forms, and pay the registration fee. Responses notifications, and the certificate of incorporation from the companies' office are sent by e-mail. While incorporating a company, an applicant can, at the same time, register online for the Goods and Services Tax and apply for a company Inland Revenue Department number. See *Ease of Doing Business in New Zealand*, THE WORLD BANK, at <https://perma.cc/24BF-PRW7>.

38. According to the Doing Business Report, Kenya's improvement in the "starting a business" segment resulted in a change in rank of 34 places from 2016 to 2017. See *Ease of Doing Business in Kenya*, THE WORLD BANK, at <https://perma.cc/6J86-4EJT>. Additionally, the United Nations Commission on International Trade Law (UNCITRAL) is currently developing a legislative guide for registration of businesses, which is deemed particularly useful for emerging economies. See United Nations Commission on International Trade Law, *Report of Working Group I (MSMEs) on the work of its twenty-eighth session* (New York, 1-9 May 2017) A/CN.9/900 (Vienna, 2017), at <https://perma.cc/ECT6-EE8G>.

39. See *Ease of Doing Business in Brazil*, THE WORLD BANK, at <https://perma.cc/UN2R-Y93U>.

and, consequently, spend a considerable amount of time and money.<sup>40</sup>

The way towards facilitating incorporation procedures is not without obstacles. There are many powerful stakeholders and pressure groups who may wish to perpetuate the status quo, as there is a lot to gain by maintaining the rents derived from formalistic procedures, which require third party intervention. José Mendoza points out the political economy problem associated with the powerful influence of such groups:

Local institutional arrangements can produce significant benefits for interest groups. These groups can easily coordinate their actions in order to block any changes to the institutions from which they obtain these benefits, regardless of whether reform would also enhance overall welfare. Resistance to institutional reform can manifest itself through the open obstruction of legislative initiatives or by subtler tactics such as the promotion or acceptance of ineffective rules.<sup>41</sup>

However, this rent-seeking phenomenon is not specific to Latin American or other emerging jurisdictions. As noted by Jesper Lau Hansen, the EU has also faced opposition from certain sectors against the simplification of corporate law:

Besides the natural tendency of vested interest to uphold the status quo, the system of notaries is often lauded for being efficient, fairly inexpensive and an important safeguard that may also guide the founders of the company on difficult questions of company law. For these reasons, the [*Societas*

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40. See REYES, *supra* note 10. As already discussed, the formalistic traits of the region's legal tradition are rooted in the colonial period. Procedures and ritualism for incorporation of business associations have been in place ever since. This fact is shown in the early presence of the notary publics, which were also referred to as "scribes." See MATTHEW C. MIRROW, *LATIN AMERICAN LAW—A HISTORY OF PRIVATE LAW AND INSTITUTIONS IN SPANISH AMERICA* 75 (U. of Texas Press 2004); Mirrow notes that during colonial times, in order to incorporate "[t]he members needed to sign an agreement (*estatutos*) before two witnesses and a scribe."

41. José Miguel Mendoza, *Convergence, Coordination and Collusion in Securities Regulation: The Latin American Integrated Market*, in *LAW AND POLICY IN LATIN AMERICA: TRANSFORMING COURTS, INSTITUTIONS, AND RIGHTS*' (Pedro Fortes, Larissa Boratti, Andrés Palacios Lleras, & Tom Gerald Daly eds., Palgrave Macmillan 2017), available at <https://perma.cc/B8ND-LZDC>.

*Unius Personae*] proposal has already encountered considerable opposition from jurisdictions accustomed to notaries.<sup>42</sup>

In addition to the time consumed by registration formalities, the process also involves fees. The following Table shows the regional ranking of costs and number of days needed for both men and women to set up a business venture.

**Table 2.** Time and Costs Required to Set Up a Business—World Bank Doing Business Index<sup>43</sup>

Economy	Time - Men (days)	Cost - Men (% of income per capita) <sup>▲</sup>	Procedure - Women (number)	Time - Women (days)	Cost - Women (% of income per capita)
<b>Region</b>					
OECD high income	8.3	3.1	4.8	8.3	3.1
Europe & Central Asia	10.2	4.7	4.9	10.2	4.7
South Asia	15.4	13.4	8.2	15.6	13.4
East Asia & Pacific	23.9	19.0	7.1	23.9	19.0
Middle East & North Africa	20.2	26.3	8.6	20.9	26.3
Latin America & Caribbean	31.6	31.5	8.3	31.6	31.5
Sub-Saharan Africa	27.3	54.0	7.9	27.5	54.1

Pursuant to the same index, Latin America and the Caribbean are currently second to last in terms of incorporation costs and time required to set up, with only Sub-Saharan Africa behind. Breaking down the above data, the World Bank calculates the cost of incorporating as a percentage of a person's income per capita. For example, in Mexico a person spends 19 percent of their annual income in paying for incorporation expenses.<sup>44</sup> In comparison, a person in

42. Jesper Lau Hansen, *The SUP Proposal: Registration and Capital (Articles 13–17)*, 12 EUR. COMPANY & FIN. L. REV. 179 (2015).

43. *Starting a Business*, THE WORLD BANK, at <https://perma.cc/K52H-G5GK>.

44. *Starting a Business: Mexico*, THE WORLD BANK, at <https://perma.cc/VA38-G5H7>.

New Zealand would only have to pay 0.3 percent.<sup>45</sup> This comparison provides an insight into the differences in jurisdictions that have implemented best practices, and those that are still lagging behind. In this vein, it provides a route for reform.

*2. Restrictions to Freedom of Contract and Dichotomy of Private Law*

The second issue with Latin American company laws is the range of unwarranted restrictions to private ordering. The region inherited the Napoleonic codifications, in which, following the 19th century liberal approaches, the parties were supposed to be granted great latitude to govern their legal relationships.<sup>46</sup> Notwithstanding this, the concept of freedom of contract appears to be very restrictive, particularly in the field of Company Law.<sup>47</sup> Several provisions of public order (*ordre public*) concerning all aspects of corporate governance can be found when reviewing legislation throughout the region.<sup>48</sup> These include, among others, mandatory rules on minority shareholders' rights, structural changes, functioning of corporate bodies, mergers, dissolution, and liquidation. The result of this legislative trait is a rise in transaction

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45. *Starting a Business: New Zealand*, THE WORLD BANK, at <https://perma.cc/H2UC-BXCW>.

46. However, even in France, the principles of economic liberalism, which were embraced in the 19th century Act of July 24, 1867 on Company Laws (*Loi du 24 juillet 1867 sur les sociétés commerciales*) were harnessed after the 1920s. According to Pierre-Henri Conac, the 1929 crisis resulted in a general questioning of economic liberalism in favor of a large degree of state intervention in the economy, which was justified by the market failures, as well as a reduction in the freedom of enterprise which was subject to a highly directory legislation. Pierre-Henri Conac, *La société par actions simplifiée une révolution démocratique*, in *LA SOCIÉTÉ PAR ACTIONS SIMPLIFIÉE : BILAN ET PERSPECTIVE 3* (Pierre-Henri Conac & Isabelle Urbain-Parleani eds., L.G.D.J. 2016).

47. This may be the result of the deeply rooted formalism inherited by the region from colonial times. As Mirrow notes, commenting on the excessive regulation of business associations: "In general, the colonial market was highly regulated by both royal law and commercial practices." MIRROW, *supra* note 40, at 76.

48. The above analysis of excessive formalities in Latin America is in sharp contrast with other jurisdictions such as Delaware, where most corporate law rules are embodied in default provisions, which may be opted out by the parties. See ROBERTA ROMANO, *THE GENIUS OF AMERICAN CORPORATE LAW* (AEI Press 1993).

costs and legal uncertainty. The following paragraphs explain this point further.

Mandatory rules in company law are all pervasive in the region. Consequently, private parties are not always able to adjust their contractual clauses to their particular needs.<sup>49</sup> Parties and their advisors have to find loopholes and other devices to circumvent certain restrictions, which may seem anachronistic today. A short-term solution found by parties may be to adopt schemes that tend to include simulated contracts that do not fully reflect the business reality. As a result of these contractual solutions, there is an increase in transaction costs, not to mention the uncertainties arising from such schemes. Moreover, simulated provisions may even be considered wrongful and subject to judicial scrutiny.

An example of this type of situation is shown in the participation of straw men in the process of incorporation whenever the legislation requires multiple shareholders in order for limited liability to exist. This requirement is contrary to contemporary business practice in which there may be situations where the sole shareholder is better suited for certain ends. Company laws throughout the region are deeply rooted in ancient legal concepts. The following can explain this trait<sup>50</sup>: the Roman law concept of *societas*, which was later developed into different forms of business entities, was strongly grounded upon a contractual foundation.<sup>51</sup> Later, the French Commercial Code maintained the idea whereby all forms of business associations arise out of an agreement between two or more persons.<sup>52</sup>

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49. See REYES, *supra* note 10, at 18.

50. *Id.*

51. Within the classification undertaken by the Roman jurist Gaius, the *societas* was included as the last of the so-called *consensu* contracts. See PASCAL PICHONNAZ, *LES FONDEMENTS ROMAINS DU DROIT PRIVE* 512 (Schultess Verlag 2008). The *societas* contract required, *inter alia*, the participation of two or more persons. See *id.* at 513.

52. In spite of this characteristic, the French, primal creators of the contractual theory, have now fully accepted the benefits derived from the flexibility of the French *Société par Actions Simplifiée* (SAS):

[The SAS] represents a major breakthrough for French Law, given the fact that it is the first time that the legislation accepts a single member business corporation in which the capital is divided into shares. It is easy to understand the success of this corporate entity in light of the freedom provided to the shareholders by the legislation, to define the internal

The transplantation of the Napoleonic codifications into Latin America resulted in the inception of a full-fledged contractual theory throughout the region.<sup>53</sup> Although the experience of several jurisdictions around the world has shown the benefits of the sole shareholder scheme and the limitations of the strict contract theory,<sup>54</sup> surprisingly, some sectors of Latin American academia still desperately cling to trite formalism.<sup>55</sup> The result has been the wide-

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rules for the company, and the suppression of a minimum capitalization requirement.

María-Beatriz Salgado, *La société par actions simplifiée: una estructura diferente en el derecho de sociedades*, in SOCIEDADES MERCANTILES, *supra* note 25, at 349.

53. For Colombia, *see* CÓDIGO DE COMERCIO (Commercial Code) art. 374 [C. COM.]; whereby traditional corporations “may not be formed or start operation with less than five stockholders.” *See id.* at art. 98:

By means of the company contract, two or more persons undertake to make a contribution in cash, work, or in other goods representing currency, for the purpose of sharing in the profits derived from their enterprise. On legal formation of a company, it will turn into a juridical person distinct from each individual shareholder.

54. For a long time, the European Union has recognized the benefits of the single member corporation. This trend has found a recent formulation in the *Societas Unius Personae*:

One of the most recent initiatives adopted by the European Commission in 2014 is the proposed Directive on the Sole Proprietor Limited Liability Company, which includes as its highlight the ‘*Societas Unius Personae*.’ Said proposal seems to be an alternative to other initiatives, focused on the importance of the European MSME’s in strengthening the EU economy.

Linda Navarro Matamoros, *Tipología societaria y derecho de la Unión Europea*, in SOCIEDADES MERCANTILES, *supra* note 25, at 307. The aim at which the *Societas Unius Personae* Directive geared is similar to that of the Model Law. It is noteworthy that both initiatives focus on MSMEs and have an additional purpose of furthering economic integration and harmonization:

The proposal by the European Commission of a directive on single-member private limited liability companies of 9 April 2014 is designed to facilitate cross-border activities of enterprises, especially small and medium-sized enterprises (SMEs) by requesting Member States to provide a company form called the *Societas Unius Personae* (SUP) that would be set up online and would follow harmonised rules on key issues.

Pierre-Henri Conac, *The Societas Unius Personae (SUP): A “Passport” for Job Creation and Growth*, 12 EUR. COMPANY & FIN. L. REV. 140 (2015).

55. For an example of this trend, *see* NÉSTOR H. MARTINEZ NEIRA, CÁTEDRA DE DERECHO CONTRACTUAL SOCIETARIO ch. 2 (2d ed., Legis 2014). Contrast this stance with the forward looking comments by another Colombian scholar, Jorge Oviedo Albán:

Under Colombian Law, by allowing for the creation of single member entities under the simplified corporations, it is no longer correct to refer now to the ‘corporate contract.’ Today, it is more appropriate to refer to

spread prohibition of the single member corporation, making it cumbersome for multinational companies and investors alike to have a presence in these countries, as they would have to associate with other persons or firms in order to carry out the investment.<sup>56</sup>

Another problem brought about by the restrictions to freedom of contract is standardization. Disregarding the importance of private ordering, hinders the development of flexible and useful legal schemes that foster innovation and creativity. Consequently, the activity of setting up a business entity is reduced to a box ticking and blank filling exercise,<sup>57</sup> to the detriment of legal innovation involved in modern business practices, which require a higher level of flexibility.<sup>58</sup>

In addition to reducing mandatory provisions, the simplification process heralded by the Model Law also results in reducing transaction costs by eliminating the outdated dichotomy of private law throughout the region (meaning the presence of both a civil code and a commercial code for the ordering of private matters).<sup>59</sup> Indeed,

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the ‘corporate juridical act,’ bearing in mind that this concept encompasses both contractual corporations and also sole shareholder entities. Albán, *supra* note 25, at 182.

56. Naturally, an investor can always set up several subsidiaries outside of the Latin American region in order to cope with the multiple member requirement. This procedure will entail significant costs.

57. For instance, legal information services providers, such as Lexis Nexis (or in the Latin American region, Legis), have established form articles of association for use by the public in setting up their corporations. For the Legis models applicable to Latin America, see *Minutos y Modelos*, LEGIS, <https://perma.cc/6C7R-GMRY>.

58. For example, this situation is contrasted with the French SAS, which is the corporate vehicle preferred by tech startups. See Francisco Reyes & Erik P.M. Vermeulen, *Company Law, Lawyers and ‘Legal’ Innovation: Common Law versus Civil Law* (Lex Research Topics in Corporate Law & Economics Working Paper No. 2011-3, 2011).

59. The dichotomy of private law in Latin America, although currently embodied in two sets of codifications as transplanted from Napoleonic law, has deep roots in the region, dating back to colonial time: “Just as the regime of contract law was divided amongst the various important sources of civil, commercial, and public law, so too was the organization and operation of the various forms of business associations.” MIRROW, *supra* note 40, at 75. Furthermore, it is interesting to note the dispersed and sometimes contradictory nature of statutory rules in the region. Mirrow further notes that in the context of laws regulating business associations, “[t]he *Siete Partidas* shared their authority in guiding companies with the *Ordenanzas de Bilbao*, which often provided somewhat different rules.” *Id.*

most codes and corporate statutes in the region have maintained a differentiation between civil and commercial companies following the French 19th century model, whereby separate substantive rules apply according to the nature of the business company.

Scholars from civil law jurisdictions have commented on this point:

In Chile the criteria to classify a firm as either civil or commercial is related to the definition set forth in its business purpose. Therefore, Article 2.059 of the Civil Code mandates that ‘the corporation may be either civil or commercial. Commercial corporations are those that are formed to carry out commercial acts, classified as such by the Law. The remaining entities are civil corporations.’ Pursuant to the quoted cited article, the classification of a corporation as commercial is framed within an external criterion relating to purpose clause as set up in the by-laws, at the moment of incorporation. If the business purpose entails carrying out any of the acts regarded as commercial by Article 3 of the Commercial Code the corporation shall be commercial, regardless of the actual business undertaking carried out by the corporation.<sup>60</sup>

The elimination of this useless differentiation for the simplified corporation increases legal certainty in the simplest way possible: parties may now be assured of which law applies, without incurring either expensive advice or illegality. This certainty reduces transaction costs.

### *3. Multiple Piercing the Corporate Veil Hypotheses*

The third issue found in the legislation throughout Latin America is the growing number of exceptions to the principle of limited liability. The issue is so problematic that according to some scholars, for example in Brazil, piercing the corporate veil has become the rule instead of the exception.<sup>61</sup> Commenting on this legal trend of reducing limited liability, Bruno Salama notes the following:

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60. María Fernanda Vásquez Palma, *Sobre los tipos de sociedades en el Derecho Chileno*, in *SOCIEDADES MERCANTILES*, *supra* note 25, at 147.

61. In this regard, *see* KRAAKMAN ET AL., *supra* note 6, at ch. 5.

In the period after the adoption of the 1988 [Brazilian] Constitution, the principle of limited liability was radically adjusted. Statutory rules and judicial decisions questioning the asset partitioning between the firm and its members were issued in virtually all areas of law (including labor law, tax, corporate and even consumer protection, as well as administrative and criminal law). Said decisions reached third parties related to the firm, including directors, contractors or counselors, and sometimes even persons having no contractual relationship with the firm, such as counsel to the shareholders. In this manner, the basic focus of the legal system shifted from protection of entrepreneurs, to protection of creditors. The pendulum moved.<sup>62</sup>

The erratic case law sometimes encountered throughout the region is mainly based on situations or regulation arising outside the scope of corporate law. Continuing with the Brazilian example, consumer protection laws contain a provision for the disregard of the corporate personality whenever the judge finds certain wrongful use of the corporate form, in the event of bankruptcy, or even whenever it is found that the corporate personality is “somehow a hindrance to the reimbursement of losses caused to consumers.”<sup>63</sup> However, even more noteworthy from the Brazilian case is that the courts have applied “unlimited shareholder liability in favor of workers by analogy to consumer protection legislation.”<sup>64</sup> Thus, in Brazil not only is there specific legislation on certain causes that may result in veil piercing, but the courts have also applied this remedy on the grounds of additional unrelated matters.

The situation is not limited to Brazil. In Colombia, for example, a judicial decision from 1992 extended liability for labor obligations to shareholders of limited liability companies,<sup>65</sup> notwithstanding the fact that the Commercial Code explicitly provided for a system of

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62. BRUNO SALAMA, *O FIM DA RESPONSABILIDADE LIMITADA NO BRASIL: HISTÓRIA, DIREITO E ECONOMIA* 26 (Malheiros 2014).

63. Unofficial English translation of article 28 of the *Código de Proteção e Defesa do Consumidor* (Consumer Protection Code).

64. KRAAKMAN ET AL., *supra* note 6, at n. 41.

65. Corte Suprema de Justicia [C.S.J.] [Supreme Court], Sala de Casación Laboral. Nov. 26, 1992.

limited liability for this type of entity.<sup>66</sup> Additionally, a different decision from the Constitutional Court appears to have extended liability arising from pension obligations of the subsidiary to a parent company, for the mere fact of being the parent.<sup>67</sup> The trend to hold parent companies liable is also present in legislation throughout the region.<sup>68</sup>

To be sure, piercing the corporate veil is a valuable remedy in corporate law. It cures wrongdoing by controlling shareholders and the abuse of the principle of limited liability. However, when this solution is extensively applied by courts without sufficient justification, it gives rise to legal uncertainty and distrust in the corporate form.<sup>69</sup> Seen in this light, the proliferation of exceptions (both statutory and judicial) to limited liability throughout the region may have the effect of discouraging local and foreign investment.<sup>70</sup>

In order to prevent these types of situations, the initiative advocates for a sound balance between the principle of limited liability, clearly incorporated in Article 2 of the Model Law,<sup>71</sup> and a narrow instance of veil piercing, applicable only when the simplified corporation is used for the purpose of committing fraud or any other wrongful act, as stated in Article 41.<sup>72</sup>

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66. Article 353 of the Colombian Commercial Code [C. COM] reads as follows: “the shareholders of a Limited Liability Company shall be liable up to the amount of their contributions.”

67. See Corte Constitucional [C.C.] [Constitutional Court], Sentencia SU-1023, Sept. 26, 2001. However, more recent decisions from the same court appear to have produced more certainty by upholding the principle of limited liability of corporations.

68. REYES, *supra* note 10, at n. 21, includes the following summary of legislation: for Brazil, *see* Law no. 6.404, art. 246; for Argentina, *see* Law no. 24.522, art. 161; and for Colombia, *see* Law no. 1116, 2006, arts. 61, 82.

69. Bainbridge has argued that the doctrine of piercing the corporate veil should be abolished, due to its uncertainty and lack of predictability increasing transaction costs for small businesses. Stephen M. Bainbridge, *Abolishing Veil Piercing*, 26 J. CORP. L. 470 (2001).

70. For an argument against the doctrine of disregarding the corporate veil, in the context of Colombia, *see* Enrique Gaviria Gutiérrez, *Contra el Disregard*, in GRANDES TEMAS DEL DERECHO COMERCIAL MODERNO: SU INCIDENCIA EN LA CONSTITUCIÓN DE 1991 (Diké 1993).

71. *See* Model Law, *supra* note 1, at art. 2.

72. *Id.* at art. 41.

#### 4. *Difficult Access to Information Subject to Public Record*

The fourth issue brought about by legislation in the region is the limited role of mercantile registries. In this geographic area, the concept of commercial publicity is deemed important in order to provide legal certainty for acts of business persons.<sup>73</sup> However, the effect of registration in the corporate sphere is restricted to publicity. In several cases the act of registration does not by itself result in the formation of a corporate body. In fact, additional bureaucratic steps are needed in order for a business to acquire legal personality. Aside from the registration, certain laws in the region frequently require notarization and sometimes even governmental authorizations. However, the recent trend in modernization of corporate law throughout the world has resulted in legislation, which derogates cumbersome multiple incorporation steps.<sup>74</sup>

Additionally, the technology used is generally obsolete and access becomes complicated. Once again, high transaction costs surface in this area. Formal registration is so complicated that the process cannot be completed without the intervention of third parties, particularly lawyers, making it even more costly, bureaucratic, and less efficient.<sup>75</sup> Additionally, this matter is plagued with stern oppo-

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73. See REYES, *supra* note 10, at n. 77 (discussing the different regulations in certain countries in the region); for Brazil, see CÓDIGO CIVIL (Civil Code) art. 993 [C.C.]; for Mexico, see Ley General de Sociedades Mercantiles [General Law of Business Associations] art. 5; for Argentina, see Law no. 19.550, art. 12; and for Colombia, see C. COM. art. 112.

74. Commenting on the trend to reduce formalism, José Miguel Embid notes that:

[A]side from the fact that [the simplification process] results in eliminating the effect of several corporate law institutions, which have been developed over a long time (such as the irregular company and the nullification of incorporation, among others), this simplification process reveals that only in the context of closely held corporations that the system electronic incorporation acquires true meaning and effect.

José Miguel Embid, *El significado de la tipología societaria en el derecho de sociedades*, in SOCIEDADES MERCANTILES, *supra* note 25, at 49.

75. The World Bank *Doing Business* report for 2016 discusses the most common problems with registration systems, which require third party intervention: “Hiring a lawyer is most common in Latin America and the Caribbean—while

sition to change the status quo. There is a multimillion-dollar business behind formal registration of firms, making it harder to break the pattern of formalization in order to achieve simplification of procedures.

The Model Law initiative firmly states that incorporation should be simple and straightforward. This idea is particularly strong in light of the empirical evidence showing that economies with third-party involvement in the process of incorporation have more businesses operating in the informal sector.<sup>76</sup> Thus, the aim of contributing to the formal economy is partly achieved by simplifying this process.

According to the World Bank, the golden principle is *minimum human intervention*.<sup>77</sup> By removing the participation of people and creating a more automatized process, the business owner by herself will be able to carry out the procedures to set up a new firm formally. The World Bank has analyzed highly inefficient legal systems in which the process of incorporation is as complicated as it is costly and prepared a graph (Figure 3) that depicts a collection of extremely complicated steps required for business formalization, evidencing a maximum degree of human intervention.

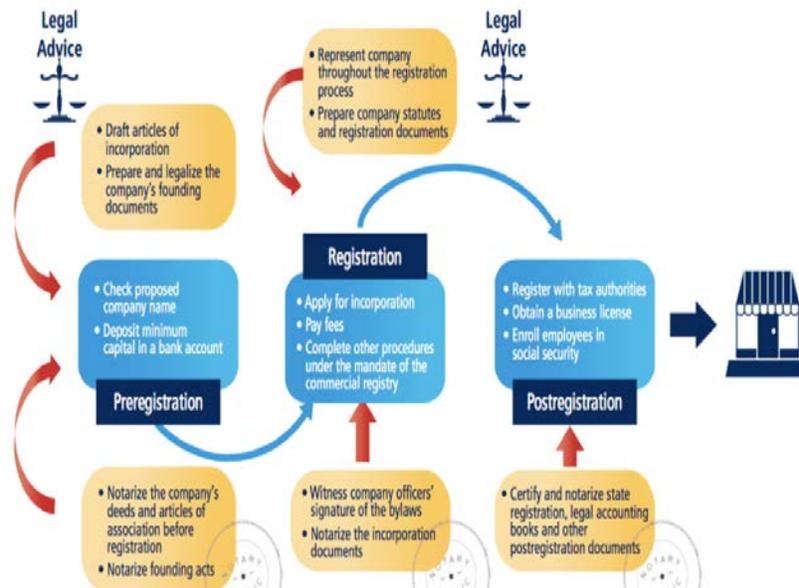
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using a notary's services is most common in Sub-Saharan Africa, Latin America and the Caribbean and the Middle East and North Africa." The World Bank, *Doing Business 2016 Report* (2016), available at <https://perma.cc/DDX2-XDGB> [hereinafter *Doing Business 2016 Report*].

76. *Id.* As shown in the *Doing Business* report data, high costs for business incorporation, especially those incurred through third-party involvement, can drive entrepreneurs to choose to operate in the informal sector.

77. See the *Doing Business* report for 2017, arguing that increased trade digitalization, which minimizes human interaction, creates fewer opportunities for bribery and fraud, using the Philippines as a compelling example in the customs sector. The World Bank, *Doing Business 2017 Report* (2017), available at <https://perma.cc/Q3S6-AUYQ> [hereinafter *Doing Business 2017 Report*].

**Figure 3.** World Bank—Procedures for Incorporation Including Human Intervention<sup>78</sup>



An example of the cumbersome ritualism in Latin American company law is the resolution rendered by a former Inspector of Justice in Argentina, according to which, parties to a corporate contract had to prove that the paid-in capital had been contributed to the company through the delivery of cash to the corporate officer.<sup>79</sup>

78. *Doing Business 2016 Report*, *supra* note 75.

79. The Argentinian Inspection of Justice is an agency entitled with the supervision of business corporations in the city of Buenos Aires. The Inspection is empowered to issue resolutions concerning the formation and operation of business corporations within that region. Proof of actual capital contributions must be brought before the National Inspection of Justice. General Resolution no. 7 of 2005 describes a rather unusual requirement for this purpose. According to its wording:

The payment [of capital] must be accredited in the legal proportion determined in the act of incorporation. Evidence of payment must be provided by deposit with the Argentinian National Bank . . . . Alternatively, proof of payment may also be provided through: 1. The explicit assertion by a notary public, in the public deed of incorporation, stating that the shareholders have effectively delivered the capital to the firm's directors, in the presence of the notary public. Alternatively, the public deed may contain an assertion in the sense that the capital has been delivered to the notary public herself, with the further obligation of transferring said funds to the firm's directors, after formal incorporation has taken place . . . .

This procedure had to be certified by a notary public. In the alternative, the parties were bound to deposit such capital contributions in the National Bank. This is contrasted with the example of New Zealand or Kenya, as already discussed, where registration is carried out online and is completed within only a few hours.

### 5. Enforcement Failure

The fifth problem posed by Latin American legislation is the lack of effective enforcement mechanisms throughout the jurisdictions in the region. This situation can be analyzed under the prism of Roscoe Pound's seminal ideas. At the beginning of the 20th century, Pound posed the question of legal efficiency by contrasting law in the books with law in action.<sup>80</sup> The empirical observation in Latin America shows the obsolescence of the court system.<sup>81</sup> As a consequence, judicial enforcement of contracts is highly inefficient.<sup>82</sup> One of the prime causes of the region's judicial delays is the fact that the law is overly ritualistic and plagued with several procedural devices that allow parties to challenge almost every decision that is rendered. As a result, the processes are lengthy and their outcome is highly uncertain. This situation gives rise to a significant degree of unpredictability and requires parties to design contractual provisions that are self-enforcing, outside of the ordinary court system.

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*Resolución General de la Inspección General de Justicia*, in *Nueva Regulación de la Inspección General de Justicia*, Resolución Número 7 de 2005 y anexos (Aug. 23, 2005), Ediciones Gari, 2006, at 95.

80. See Roscoe Pound, *Law in Books and Law in Action*, 44 AM. L. REV. (1910).

81. See *Doing Business 2017 Report*, *supra* note 77, at 190, 195, 199, 200, 224.

82. Ronald J. Gilson notes that emerging jurisdictions sometimes display a broader scope of legal deficiencies, beyond merely lacking minority protection rules:

With bad commercial law, exchange must be self-enforcing because there are neither authoritative rules nor an effective judicial system to enforce those obligations. Transactions in this circumstance take place in a reputation market, which substitutes for law (or law's shadow) as a means to assure that parties perform their contractual obligations.

Ronald J. Gilson, *Controlling Family Shareholders in Developing Countries: Anchoring Relational Exchange*, 60 STAN. L. REV. 633 (2007).

The following chart shows the difficulty of the enforcement of contracts in the region.

**Table 3.** Enforcement: Procedures, Time and Cost<sup>83</sup>

<b>Latin America</b> (selected economies)	<b>Processes</b> <b>Quality Index</b> (0-18)	<b>Time</b> (days)	<b>Cost</b> (% of claim)
Argentina	11.5	660	22.5
Brazil	13	731	20.7
Chile	9	480	28.6
Colombia	9	1,288	45.8
Mexico	9.5	350	33.5

Aside from the transaction costs imposed on parties by the *Kafkaesque* proceedings, another primal cause of inefficiencies is the fact that, normally, there are no specialized corporate law courts in the region. In general, it is fair to say that Latin American jurisdictions lack what Professor Luca Enriques refers to as “good corporate judges.”<sup>84</sup> As a result, case management is not well developed and there is no specific regulation concerning time standards for the proceedings. Additionally, court automation is underdeveloped, to say the least, causing delays by failing to make use of existing technologies to facilitate the different instances within the legal process.

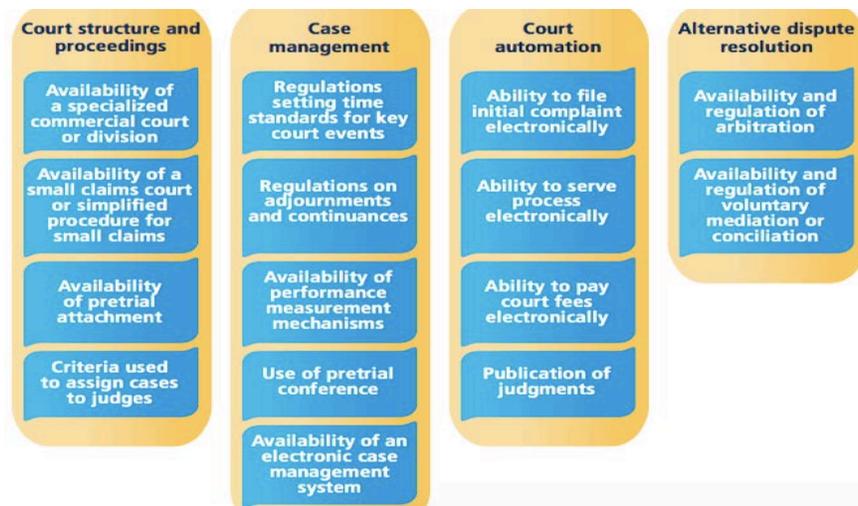
The following diagram presents the main areas of focus by the

83. *Doing Business 2017 Report*, *supra* note 77, at 190, 195, 199, 200, 224.

84. See Luca Enriques, *Off the Books, but on the Record: Evidence from Italy on the Relevance of Judges to the Quality of Corporate Law*, in GLOBAL MARKETS, DOMESTIC INSTITUTIONS: CORPORATE LAW AND GOVERNANCE IN A NEW ERA OF CROSS-BORDER DEALS 258 *et seq.* (Curtis J. Milhaupt ed., Columbia U. Press 2003). The characteristics of good corporate judges are as follows: “1. Honesty, rapidity, and expertise . . . 2. No deference in conflict-of-interest cases . . . 3. Capacity to identify real rights and wrongs . . . 4. Antiformalism . . . 5. Concern for spill-over effects.” *Id.* at 7-9. Additionally, Enriques summarizes these traits: “At the most basic level, there is widespread agreement that a certain degree of judicial honesty and effectiveness . . . are necessary elements of a sound corporate law system . . . Their absence is a real problem today mainly in developing countries . . .” *Id.* at 3.

Doing Business Index when evaluating the quality of the proceedings. The difficulties associated with the judicial system have been meticulously assessed by the World Bank in its Doing Business Report. For this purpose, the Bank carefully analyses the basic aspects that could lead to an efficient judicial system. Among the most relevant, the following factors are considered: (i) the availability of specialized courts; (ii) the regulations concerning the timeframe for each procedural instance; (iii) the access to automated systems for filing complaints and serving notices, and (iv) the existence of alternative dispute resolution mechanisms.

**Figure 4.** Areas Covered by the Quality of Judicial Processes Index<sup>85</sup>



As a result of the court inefficiency described above, costs are prohibitively high when litigating in the region, both in terms of monetary expenditure and time spent. For example, according to the Doing Business report for Mexico, in 2017 the cost of enforcing a contract before the judiciary, as a percentage of the claim, rises to 33.5 percent.<sup>86</sup> As a consequence, a contracting party wishing to have its contract enforced will lose almost half of the amount

85. *Doing Business 2016 Report*, *supra* note 75.

86. See *Ease of Doing Business in Mexico: Enforcing Contracts*, THE WORLD BANK, at <https://perma.cc/P2AH-9ZHF>.

claimed in the court proceedings (if successful).<sup>87</sup> The difference between law in books and law in action throughout the region is described by the distinguished scholar Robert Charles Means in the following excerpt: “the tendency for Latin American countries to enact laws with little regard for social reality and less for effective implementation is well known . . . . This kind of isolation of legal rules from reality might be called enforcement unreality.”<sup>88</sup>

In the same vein, Bruno Salama and Viviane Muller describe this scenario, capturing many of the problems present throughout the region by using Brazil as an example:

Brazilian courts are largely deemed by corporate lawyers and other market players to lack the necessary expertise to delve into the intricacies of securities laws and the economic dynamics of securities transactions. This trait can be partly attributed to the absence of courts and judges specialized in corporate and securities transactions. In fact, Brazilian courts are remarkably slow and their decisions on corporate matters are somewhat unpredictable.<sup>89</sup>

#### 6. *Costs of Starting a Business*

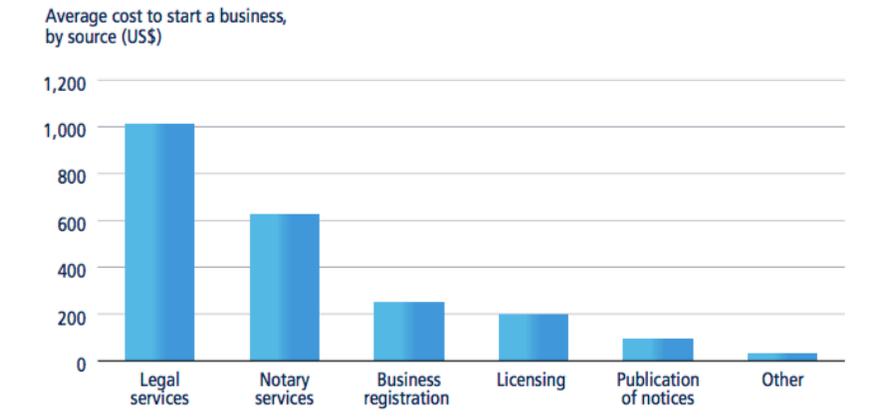
Another problem with the current legislative approach is the expense associated with the creation of a business. Figure 5 below shows the average cost related to starting a business by focusing mostly on bureaucratic expenses that the entrepreneur must incur in order to set up a formal business structure. As may be seen from the graph, the costs of incorporating in the region are significant. This situation is particularly worrisome when bearing in mind that business startups already require large amounts of capital up front. Businesspersons should not have to divert their scarce resources into complying with bureaucratic formalities. It is noteworthy that the highest costs seen below do not relate to the operation of the business itself, but are solely incurred in legal formalities.

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87. Obviously, if the claiming party is not successful, she would spend the equivalent to half of her claim and a significant amount of time.

88. See ROBERT CHARLES MEANS, UNDERDEVELOPMENT AND THE DEVELOPMENT OF LAW: CORPORATIONS AND CORPORATION LAW IN NINETEENTH-CENTURY COLOMBIA 151 (U. of North Carolina Press 1980).

89. See Salama & Muller, *supra* note 30, at 178.

**Figure 5.** The Costs of Opening a Business<sup>90</sup>

This situation is in contrast with more advanced systems in which businesspersons are able to focus their resources (financial and other) on developing their business, rather than in complying with costly formalisms. Therefore, in many cases there is no need to resort to lawyers and other professionals in order to complete the incorporation process.

### III. CONTENTS OF THE MODEL LAW

The Model Law is inspired by the Colombian SAS. Reference to the Colombian experience is, thus, crucial in understanding the main aspects of the initiative. In December of 2008, the Colombian Congress enacted Law 1258 of 2008, creating this new type of business. The Colombian law contains elements found in corporate law coming from both the common law and civil law traditions. In fact, the basic structure and contents of the law are based on the French legislation on the *société par actions simplifiée*.<sup>91</sup> Additionally, certain American law elements, mainly from the state of Delaware,

90. *Doing Business 2016 Report*, *supra* note 75.

91. The original legislation of the French SAS was enacted in 1994 (Law no. 94-1, Jan. 3, 1994). Several reforms followed to make it even more flexible and simplified. For an overview of this type of business entity, *see* PIERRE-HENRI CONAC & ISABELLE URBAIN-PARLEANI, *LA SOCIÉTÉ PAR ACTIONS SIMPLIFIÉE (SAS)* (Daloz 2016).

were also included in the statute.<sup>92</sup> The result is a closely held corporation that resembles the so-called unincorporations that have been introduced into the United States, the United Kingdom and some civil law jurisdictions.<sup>93</sup>

It is also noteworthy that there have been other similar laws introducing regulation on simplified closely held corporate vehicles in Latin America. The first legislation of the sort was the Chilean Law 20.190 of June 5, 2007. According to Chilean commentator María José Viveros Bloch, this legislation was aimed at allowing the small business owner to formalize her venture.<sup>94</sup> On the other hand, Mexico enacted a law on December 9, 2015 regarding *sociedades anónimas simplificadas* (simplified corporations). The most recent case is the Argentinian adoption of the *sociedad por acciones simplificada* with Law 27.349,<sup>95</sup> which incorporated in the law designed to encourage entrepreneurship (Title 3). There is also draft legislation on various types of similar business entities in Brazil.

By providing a combination of corporate and partnership-like components, the Colombian SAS allows for significant contractual flexibility, while still preserving the benefits of limited liability and asset partitioning. As an example, some of the partnership-like features include simple formation procedures, internal flexibility and share transfer restrictions. These features allow businesspersons to cope better with agency problems within the corporations in which management has been delegated.<sup>96</sup> On the other hand, certain crucial

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92. See ROMANO, *supra* note 48.

93. See Reyes & Vermeulen, *supra* note 58; see also RIBSTEIN, *supra* note 6.

94. See MARÍA JOSÉ VIVEROS BLOCH, *SOCIEDAD POR ACCIONES: ANÁLISIS DE UN NUEVO TIPO SOCIAL 44* (Librotecnia 2006) (for the summary of the Chilean law's objectives).

95. Published in the Official Bulletin on Apr. 12, 2017.

96. By allowing a higher degree of contractual flexibility, parties are enabled to set up devices aimed at defining *ex ante* each of the corporate participants' obligations and rights. This latitude is oriented towards the completion of the corporate contract, reducing the potential for exposed disputes. For a discussion regarding the incomplete contract theory, see Robert E. Scott & George G. Triantis, *Incomplete Contracts and the Theory of Contract Design* 56 CASE W. RES. L. REV. 187 (2005).

corporate features, like having a separate legal personality and continuity of life, have also been kept.<sup>97</sup>

The Model Law contains a total of 43 articles regulating all stages in the life span of the corporation. As with any other model law, its provisions are intended to serve as a guide for legislators and policymakers alike. Therefore, they can be adapted in order to make them compatible with domestic legislation. The following is a short discussion of the main traits of the Model Law, inspired by the Colombian SAS.

#### *A. Facilitating Incorporation Procedures*

Following an Anglo-American approach to corporate law, the Model Law significantly reduces formalities for incorporation. Many of the proceedings existing in Latin American countries are reminiscent of ancient formalities that have been abandoned in other jurisdictions. Therefore, streamlining the requirements to set up the business by removing some of these cumbersome steps is not incompatible with legal certainty. Interestingly, the latter goal can be reached through a simple filing procedure before a public registry (such as a chamber of commerce).

Article 5 of the Model Law reads as follows: “A simplified stock corporation will be formed by contract or by the individual will of a single shareholder, provided that a written document is granted. The formation document shall be registered before the Mercantile Registry . . . .”

The same article also lists a total of seven items, which normally form part of the incorporation document.<sup>98</sup> This requirement is not intended to create an unjustified burden on the parties, but instead is aimed at the disclosure of basic corporate information. The article contains minimum legal requirements such as the corporation’s domicile, its name, and the subscribed capital, among a few others. It is basic information designed to identify the business entity, so

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97. These characteristics allow for limited liability and indefinite duration of the business enterprise.

98. See Model Law, *supra* note 1, at art. 5.

that third parties can deal with it confidently. The same Model Law provision categorically mandates that “no additional formalities of any nature shall be required for the formation of the simplified stock corporation.”<sup>99</sup> Even more significant is the removal of the notary public’s intervention in the process. This recommendation is geared towards the suppression of intermediaries and the reduction of unnecessary costs (including monetary and time related expenses).

Furthermore, the Model Law provides certainty as to when legal personality arises. Article 3 states that “[u]pon the filing of the formation document before the Mercantile Registry . . . , the simplified stock corporation will form a legal entity separate and distinct from its shareholders.”<sup>100</sup> This simplification is intended to settle the discussion concerning the precise moment in which the legal personality is acquired. Where the law requires several different steps for the incorporation to be completed, as is frequently the case in Latin America, it becomes difficult to tell when the process has come to fruition. Under the Model Law, all incorporation formalities are reduced to a filing before the mercantile registry.<sup>101</sup> Such registration partly covers the functions previously served to the intervention of notary publics. Experience has shown that there is no practical need in having two sets of formal procedures (granting of a public deed of incorporation, and filing before the mercantile registry) directed towards the same end. Thus, the Model Law has granted the mercantile registry with certain attestation functions over the incorporation documents filed.<sup>102</sup> The mercantile registry shall only provide a review of the legality of the provisions set in the incorporation documents, and may only deny registration where it finds that the elements enumerated in Article 5 of the Model Law have not been included.<sup>103</sup>

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99. *Id.* at art. 5.

100. *Id.* at art. 3.

101. This feature appears in other jurisdictions, including some in the United States, whereby filing before the registry acts as a presumption as to the existence of the corporate body. *See* ABA, REVISED MODEL BUSINESS CORPORATION ACT (2006) Section 106.

102. *See* Model Law, *supra* note 1, at art. 6.

103. *Id.* at art. 8.

Following the underlying concern with simplification and cost reduction, a system of online registration should be implemented. In Colombia, certain local mercantile registries have implemented an electronic system for the formation of simplified corporation.<sup>104</sup> The system requires the incorporator to have a personal digital signature which can also be acquired through an online application system.<sup>105</sup> All these electronic devices find solid legal grounds in Colombia, given the early adoption of the UNCITRAL Model Law on electronic commerce, by Law 527 of 1999. This law incorporated the principle of functional equivalence, whereby any data message is sufficient to replace paper-based formalities at least concerning so-called private documents (i.e., those that are not subject to notarization or any other form of authentication by a public officer).<sup>106</sup>

### *B. Full-Fledged Limited Liability*

The Model Law reinforces the foundational principle of limited liability by including legal provisions directed at ameliorating the impact of the piercing of the corporate veil doctrine. Accordingly, the few exceptions to limited liability are reserved exclusively to situations where there is clear and sufficient evidence of an abusive use of the corporate form, provided that the liable party has acted wrongfully or in a fraudulent fashion.

There is an attempt in the Model Law to strike a balance between asset partitioning on the one hand, and the extension of liability to

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104. The following web page may be accessed to incorporate the simplified corporation electronically, *Constitución de Sociedades por Acciones Simplificadas (SAS)*, CAMARA DE COMERCIO DE BOGOTÁ, <https://perma.cc/5MV7-ZXEK> (under “Constitución Virtual de SAS,” follow “Constituir” hyperlink).

105. The digital signature may be acquired filing out the necessary forms in the following web page, *Adquiera o renueve su firma digital*, CERTICÁMARA, <https://perma.cc/T7AJ-J9GN>.

106. In accordance with Article 6 of Law 527 of 1999, where a legal provision requires that information be in writing, such requirement shall be complied with by means of a data message, provided that the information contained therein is accessible for its future consultation. The use of new technologies has been described by scholars as one of the factors modernizing Corporate Law: “The progressive use of new technologies has been one of the factors accompanying the process of typology renovation in the closely held corporation, with the aim of facilitating and simplifying its existence, organization and operation.” Embid, *supra* note 74, at 48.

responsible parties.<sup>107</sup> The economic rationale for the limitation of liability and the instances of veil piercing have been broadly discussed by renowned scholars.<sup>108</sup> Following the mainstream approach to these principles, one of the objectives of the Model Law in this regard is to provide an appropriate remedy for the aggrieved when the legal entity status has been severely eroded. The initiative thus intends to limit the situations for judges to hold shareholders liable for the company's obligations. Fraud or misuse of the corporate form should be the sole events to trigger judicial intervention.<sup>109</sup> There appears to be no valid justification introducing so many exceptions to the principle of limited liability. There is a willingness to counteract the wholesale disregard of the legal entity in view of the many cases where the exception to the principle of limited liability becomes the rule. This is particularly true when case law is founded to a large extent upon situations unrelated to the domain of corporate law.

The region's writs of constitutionality (*mandado de segurança* in Brazil, *acción de amparo* in Mexico and Argentina, and *acción de tutela* in Colombia) have been used on several occasions as a mechanism for piercing the corporate veil. This type of litigation threatens the economic foundations of corporate law. This way, "defending weak creditors through expeditious writs (in which the true merits of each case are not carefully assessed by constitutional courts) negatively impacts certainty and reasonable reliance on these legal systems."<sup>110</sup> The Brazilian experience must serve as an important warning for the region, given the precedents that have jeopardized the economic benefits arising from the principle of limited liability. In the opinion of Salama, the Brazilian trend of allowing

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107. See Model Law, *supra* note 1, at arts. 2, 41.

108. See among many other works: FRANK EASTERBROOK & DANIEL FISCHER, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* 40 (Harvard U. Press 1996); Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 *YALE L.J.* (1991); Bainbridge, *supra* note 69; Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 *CORNELL L. REV.* (1991); PIERRE MOUSSERON, *DROIT DES SOCIÉTÉS* 79 (2d ed., Montchrestien 2005); SALAMA, *supra* note 62.

109. See Model Law, *supra* note 1, at art. 41.

110. REYES, *supra* note 10, at 21.

the government radical involvement in the allocation and reallocation of corporate risks was eventually consolidated. As a result of that, additional legal branches were introduced to better protect the interests of certain groups. Therefore, new fields of the law appeared, such as environmental law, consumer, labor law, social security law, urbanistic law, and others.<sup>111</sup>

Similarly, it has been widely held that upholding the principle of limited liability is a plausible objective, particularly when facing voluntary creditors.<sup>112</sup> Currently there does not seem to be a major dispute on this topic. On the other hand, regarding the so-called involuntary creditors, there is an ongoing doctrinal debate as to whether the principle should also prevail in tort cases.<sup>113</sup> Notwithstanding the scholarly debate surrounding these topics, there is no differentiation in the Model Law concerning the situation just described. The legal entity can be judicially disregarded in the exceptions already discussed.

### *C. Private Ordering*

The Model Law upholds the principle of freedom of contract between private parties. This marks a defining trait of modern corporate law, particularly regarding hybrid business forms.<sup>114</sup> Upon discussing the French SAS, Périn and Germain, single out a distinctive feature of the simplified corporation which lies in the possibility to adjust internal functioning, enabling shareholders to benefit from both corporate characteristics and added flexibility: “The method of internal organization confers the SAS its originality *vis-à-vis* other types of company. The simplified corporation is a liberalized form

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111. See SALAMA, *supra* note 62, at 356.

112. See Hansmann & Kraakman, *supra* note 108.

113. *Id.*

114. Commenting the Colombian SAS legislation, local scholars note: “Today, there is consensus in Colombia of the fact that the Law 1258 of 2008 is the most important reform to Corporate Law of the last decade. The SAS was created based on the pillar of corporate flexibility by incorporating, in its majority default rules.” William Hernandez, *La sociedad por acciones simplificada en Colombia*, in *SOCIEDADES MERCANTILES*, *supra* note 25, at 204 (citations omitted).

of moral person, which includes the financial benefits from the corporate form, with a vast autonomy to define its internal powers.”<sup>115</sup>

The flexibility provided by the Model Law is characteristic of best practices from both the common law and civil law traditions. As noted above, a broad freedom for parties to define their legal relationships is pervasive in American corporate law.<sup>116</sup> Likewise, the 1994 French law on SAS, along with its numerous amendments is a good example of private ordering. According to Philippe Merle: “The novelty introduced by the SAS consists in granting absolute preponderance to freedom of contract for the shareholders, as manifested in the by-laws. The application of legal provisions may be opted out of by contracting parties.”<sup>117</sup>

As has already been explained, the simplified corporation introduced by the Model Law is barred from listing its securities in a stock exchange. This is due to the need to maintain the Model Law regulation as flexible and enabling for businesspersons. In fact, keeping it away from the securities markets removes the difficult issues concerning the protection of dispersed investors as there is a close relationship between ownership and control in the simplified corporation.<sup>118</sup>

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115. PIERRE-LOUIS PÉRIN & MICHEL GERMAIN, *SAS - LA SOCIÉTÉ PAR ACTIONS SIMPLIFIÉE : ÉTUDES-FORMULES 3* (3d ed., Joly Éditions 2008).

116. Noting the increasing flexibility awarded to close corporations by judges and legislators in the United States, Palmiter and Partnoy state that:

For many years, planners of the close corporation confronted judicial antagonism to special arrangements—whether embodied in the articles, by-laws, or a separate agreement if they departed too far from the traditional statutory model. Two parallel developments, starting mostly in the 1960s, have substantially loosened this judicial attitude. First, courts have become more realistic about the special demands of close corporations and have become far more tolerant of departures from the norm. Second, legislatures have recognized the unnecessary rigidity of the traditional structure and have created special rules for the close corporation.

PALMITER & PARTNOY, *supra* note 31, at 1005. *See also* ROMANO, *supra* note 48; and the ABA, MODEL BUSINESS CORPORATION ACT (2006).

117. PHILIPPE MERLE, *DROIT COMMERCIAL : SOCIÉTÉS COMMERCIALES* 602 (5th ed., Précis Dalloz 1996).

118. Commenting on the approach adopted in the United States, Professor Bainbridge notes: “The regulatory regime for statutory close corporations is substantially more liberal in a variety of ways than is mainstream corporate law.” STEPHEN M. BAINBRIDGE, *CORPORATE LAW* 486 (3d ed., Foundation Press 2015).

The prohibition to offer securities on an exchange does not imply that the simplified corporation cannot be used to undertake large business projects, or that it is to be adopted exclusively by MSMEs. It is likely that the flexible capital structure is the most attractive element of the entity for large firms. This flexibility allows for different types of investors, some active and some passive, and is generally regarded as adequate for large business groups and tax planning.<sup>119</sup>

In the absence of the simplified corporation, Latin American MSMEs are subject to a challenging dilemma. On the one hand, they could choose the traditional corporate form in Latin America (generally the *sociedad anónima*), benefitting from its features, but assuming the downside of stringent rules and formalities.<sup>120</sup> On the other hand, they could adopt partnership-like entities which provide wide flexibility, but are subject to the disadvantage of unlimited liability. The simplified corporation combines the benefits from both types of business entities. Cozian notes the following regarding the French law on SAS: “The fundamental idea is to offer members of

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119. As an example of the benefits provided by this flexibility, the following is noted:

The Model Law enables the corporation to issue classes and series of shares. The distinction between these two concepts has obvious practical consequences. Share ‘classes’ refer to various categories of instruments that are differentiated on the basis of the inherent rights associated with them, according to the relevant regulation. On the other hand, the ‘series’ identify successive issues of the same class of shares, where such shares have been placed at different time periods. Finally, Article 10 of the Model Law also contemplates that the company may issue shares ‘for any consideration whatsoever, including in-kind contributions, or in exchange for labor contributions pursuant to the terms and conditions contained in the by-laws.’

REYES, *supra* note 10, at 114.

120. The French simplified corporation was partly adopted with the objective of establishing a corporate vehicle, which is free from the formalities of the classic corporation (*Société Anonyme* or S.A.):

The S.A. bears the inconvenient of requiring at least seven shareholders, and having a complex system establishing the existence of a general shareholders assembly, board of directors, and director general. None of these are required in the SAS . . . to sum up, the SAS counts with all the advantages of the classic S.A. (limited liability, share transfers etc.), without the inconveniences of said entity (minimum shareholders requirement, internal organization).

JEROME BONNARD, *DROIT DES SOCIETES* 126-127 (3d ed., Hachette Supérieur 1999).

the simplified corporation an organizational form very similar to the ‘company-contract’ (*société contrat*), where the essential functioning rules are provided by agreement between the parties. This way, the rules of the corporation (*société anonyme*) may be opted out of.”<sup>121</sup>

The initiative contains default provisions which the parties may opt into, or opt out of at their will. Consequently, business participants can implement almost any arrangement which they deem better suited to their business needs.<sup>122</sup> Some examples of these provisions in the Model Law are the possibility for shareholders to either fully define the main business activities of the corporation, or set up an open ended purpose clause whereby the corporation may engage in any lawful business;<sup>123</sup> the possibility for the corporation to have an unlimited life span;<sup>124</sup> freedom to organize the internal structure and operation of the corporation;<sup>125</sup> leeway to define voting majorities for a shareholders meeting,<sup>126</sup> among others.

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121. MAURICE COZIAN ET AL., *DROIT DES SOCIÉTÉS* 365 (18th ed., LexisNexis 2005). Périn and Germain note the following regarding the French SAS: “[A]dding freedom of contract to the creation of a corporation constitutes an unprecedented privilege in French Law. For any rational agent, incorporating her firm as an SAS corresponds to the desire to increase organizational efficiency, by having it adapt to its shareholders particular needs.” PÉRIN & GERMAIN, *supra* note 115, at 11. The same characteristic is present in the Colombian SAS whereby decision on the internal configuration of governance organs is left to the will of the shareholder(s).

122. Private ordering is an important feature introduced by the Colombian SAS law, into the previously rigid Colombian Corporate Law:

Naturally, the SAS’ opt in approach also allows for private parties to step out of the standard provisions contained in model by laws and to draft sophisticated agreements that are appropriate for more complex undertakings. The enabling non-directory provisions of Law 1258 have fostered private ordering and sparked innovation in Corporate Law across the country. Aside from the boilerplate type of agreements that are used by most start-ups, practicing attorneys are becoming skillful at developing new legal structures suitable for a more sophisticated business environment. A survey conducted with law firms and sole law practitioners in the capital city of Bogotá has allowed for the identification of several legal structures in which one or more SAS can be properly used for an unlimited number of business purposes.

Francisco Reyes, *Corporate Governance in Latin America: A Functional Analysis*, 39 U. OF MIAMI INTER-AM. L. REV. (2008).

123. *See* Model Law, *supra* note 1, at art. 5(5).

124. *Id.* at art. 5(4).

125. *Id.* at art. 17.

126. *Id.* at art. 22.

The approach based on the primacy of private ordering assumes that contracting parties will be diligent enough either to adequately negotiate the terms of the agreement so as to suit their particular needs, or to adapt by default to off the rack housekeeping rules provided in the corporate statute. Naturally, the fact that there is significant latitude for parties to define the structure of their corporation also entails a burden to prevent unintended consequences by careful negotiation of provisions from the outset.<sup>127</sup> For example, incorporators may wish to establish special supermajorities which differ from those contained as fallback provisions, in case they desire to implement their voting arrangements. Depending on the specific circumstances, parties need to carefully design their own agreement in order to fit their needs.

*D. Unrestricted Business Purpose, Perpetuity and Commercial Character*

The Model Law allows for the adoption of an unrestricted business purpose for any Simplified Corporation.<sup>128</sup> This characteristic coincides with the trend of advanced jurisdictions such as the United States,<sup>129</sup> and to a lesser extent, the EU<sup>130</sup> and the UK.<sup>131</sup> By means

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127. See STEPHEN M. BAINBRIDGE, *CORPORATION LAW AND ECONOMICS* 9 (Foundation Press 2002).

128. See Model Law, *supra* note 1, at art. 5(5).

129. Palmiter and Partnoy explain the evolution and fallout of the *ultra vires* doctrine in the United States: “In the nineteenth century, the law of corporations was mainly devoted to the resolution of disputes arising under the *ultra vires* doctrine. Today the issue rarely arises. Clearly, the original purpose of the doctrine to curb the powers of large corporations has failed, largely replaced by expanded fiduciary duties.” PALMITER & PARTNOY, *supra* note 31, at 171.

130. Commenting on the first European company law Directive, it has been asserted that:

Even though this directive notes that the corporation’s legal capacity is defined by the purpose clause as set forth in the relevant articles of incorporation, it also underscores that innocent third parties are protected vis-à-vis the validity of *ultra vires* business transactions to which they were a party—provided they did not know that the corporation lacked sufficient capacity to undertake such a transaction. Pursuant to the same directive, bad faith will not be presumed solely on the grounds that the relevant party had access to a certificate issued by the relevant company registry, in which the purpose clause is described.

REYES, *supra* note 10, at 31.

131. See the United Kingdom’s Companies Act of 2006 (c.46), at 31(1).

of this provision, the anachronistic *ultra vires* doctrine that still exists in many Latin American countries is altogether left behind. Said doctrine is supposed to protect shareholders from the presumed excess of powers which managers may sometimes arrogate upon themselves by acting beyond the terms of their mandate. According to this view, establishing limitations to the capacity of the corporation ensures that the entity will only be liable for acts that are explicitly provided for in the corporate documents.

However, modern corporate law across the board tends to disregard the usefulness of this doctrine. It has been asserted that the prohibition of *ultra vires* acts may be deemed too formalistic and detrimental to entrepreneurial activity.<sup>132</sup> This doctrine may even tend to create legal uncertainty, as it subjects contracting third parties acting in good faith, to the nullification of contracts with the corporation. In fact, the corporation can always challenge its own acts on the grounds that it lacked sufficient legal capacity to execute them.

The trend against this doctrine may also take into consideration the ownership structures prevailing in Latin America. As already explained, closely held family enterprises, with no separation between ownership and control, are common in the region. This may render the *ultra vires* doctrine useless, given the fact that shareholders may themselves assert direct control over the day-to-day running of the company.<sup>133</sup> On the other hand, the ample flexibility contained in the Model Law allows shareholders to either choose an unrestricted business purpose, or to introduce limitations thereto.

Additionally, the Model Law introduced the perpetuity of existence theory, which runs contrary to many Latin American legislations. Most corporate laws in the region have maintained a Napoleonic provision whereby a company should be created for a limited

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132. See FRANCISCO REYES, DERECHO SOCIETARIO 299 (3d ed., Editorial Temis 2016).

133. Palmiter and Partnoy however hold that there is still a place for the *ultra vires* doctrine in closed corporations; See PALMITER & PARTNOY, *supra* note 31, at 172. The present paper suggests quite the contrary: by having shareholders actively participating in the day-to-day management of the closely held corporation, their scrutiny of directors' actions renders the protection of the *ultra vires* doctrine useless.

duration.<sup>134</sup> The objective is to reduce outdated formalities and introduce more flexibility for entrepreneurs.<sup>135</sup>

The initiative also intends to put an end to the anachronistic dichotomy of private law present throughout the region. The Model Law mandates that the simplified corporation is to have a commercial nature—without regard to the objects or purposes set forth in the relevant incorporation documents.<sup>136</sup> Consequently, it becomes irrelevant to analyze whether the business association's activities have a civil or a commercial nature. This characteristic is intended to provide the maximum amount of legal certainty for shareholders and for parties contracting with the simplified corporation.

#### *E. Freedom to Define Internal Structure*

With the aim of introducing more flexibility for the benefit of businesspersons, the formation and operation of internal governance organs are also simplified in the Model Law. As well as achieving a streamlining of procedures and eliminating unnecessary bureaucracy, this characteristic arguably reduces costs for the entrepreneur.

An example of this leeway can be seen in the board of directors regulation contained in the initiative. Under the Model Law there is no statutory obligation to create a board of directors.<sup>137</sup> Even though the importance of said body for the management of corporations is acknowledged, regulatory restrictions have been loosened to the point where shareholders may even decide if they require such a board or not. For instance, small business ventures may find benefits in excluding the board altogether. This feature specifically responds to the already analyzed fact that most companies in Latin America

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134. The former art. 1865 of the French Civil Code [C. CIV.] established that the corporation would be terminated by the expiration of the term for which it was contracted (now art. 1838, Law no. 78-9, Jan. 4, 1978). The Law no. 66-537 of July 24, 1966 contained a provision whereby corporations could not be formed for a term exceeding 99 years.

135. See Model Law, *supra* note 1, at art. 5(4).

136. *Id.* at art. 1.

137. *Id.* at art. 25.

are closely held, and thus do not reflect the idea of a separation between ownership and control.<sup>138</sup>

In the event the incorporators determine that there will not be any board of directors in the corporation, both the management and direction shall be entirely allocated on the legal representative and any of her subordinates. In accordance with Article 25 of the Model Law, “in the absence of a provision requiring the operation of a board of directors, the legal representative appointed by the shareholders assembly shall be entitled to exercise any and all powers concerning the management and legal representation of the simplified stock corporation.” At the moment of incorporation or at any point during the corporation’s life span, additional committees may be created such as management, audit, or any other that the parties deem necessary.

This flexibility is not restricted to the creation of governance organs, but also to the applicable rules for their operation. There is thus ample freedom for shareholders to determine aspects such as calling of meeting, quorum, voting majorities, and shareholders’ representation, among others.<sup>139</sup>

This flexibility will be particularly beneficial for MSMEs, as their owners will have leeway to decide whether a corporate organ such as the board of directors is excluded, instead of having to set up mandatory corporate bodies with the only purpose of complying with cumbersome legal ritualism.

#### *F. Rules on Capital*

New provisions on capital and classes of stock are also included. The capital structure of the simplified corporation allows for any

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138. See GORGA, *supra* note 26 and accompanying text.

139. For example, it is clear that this freedom of determination would benefit different types of shareholding configurations. When two shareholders wish to have shared management and direction of the corporation a single-member board may prove helpful, particularly when the manager is different from the sole director. Such a system enables those shareholders to divide the corporation’s direct management by granting binding authority to the legal representative and oversight powers to the single board member. In fact, in corporations with two shareholders and symmetrical capital contributions, this may be a suitable structure because it allows the exercise of reciprocal controls.

imaginable form of equity financing. Rules are introduced, for example, to set up either ordinary or dual classes of voting shares, including multiple voting rights. Contributions in kind or in labor are also permitted in the simplified corporation. The flexibility afforded by the Model Law is in sharp contrast with formalistic restrictions on capitalization in the region. Article 9 of the SAS Model Law contains rules that are a departure from the general rule that has typically been included in commercial codes throughout Latin America. Specifically, Article 9 enables business parties to define the amounts for the corporation's authorized, subscribed and paid-in capital. Furthermore, the term provided in the Model Law for the payment of any capital contributions can be made within the following two years, from the moment in which the shares of stock were subscribed.<sup>140</sup>

An additional feature that is closer to the partnership regime than to corporate law, relates to transfer restrictions that can be included in the corporation's by-laws. In this sense, shareholders may be required to submit any transfer of shares to rights of first refusal. Additional limitations, such as the inability to convey the shares of stock for a fixed period of time can also be stipulated. Likewise, preemptive rights for the issuance and subscription of new shares can also be included in the by-laws. All these contractual devices are particularly important in the context of family owned businesses, where shareholders may wish to keep the entity as closed as possible. By setting up these types of clauses, third parties are normally denied access to ownership.

### *G. Protection Mechanisms*

The SAS Model Law contains significant protection mechanisms, which are more sophisticated and effective than those normally contained in traditional corporate law across the Latin American region. As it has been stated before, the Model Law provides significant leeway to business participants. Thus, most *ex ante* legal

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140. REYES, *supra* note 10, at 113.

devices containing restrictions to freedom of contract or setting forth prohibitions imposed upon directors, officers and shareholders, are not included in such Model Law. By means of this approach, directory regulations are replaced with default provisions, which are only applicable in the absence of specific contractual provisions.

To prevent the misuse of the corporate form, the Model Law contains legal standards aimed at the protection of shareholders and creditors. For example, as noted above, third parties are entitled to bring actions for piercing the corporate veil where there is an abusive or fraudulent use of the business entity. Additionally, minority shareholders are protected by certain causes of action intended to reduce tunneling and abuse of right.

The point of departure for this legal approach is the well-known presence of agency problems existing between controlling and minority shareholders (as opposed to the traditional dichotomy which confronts the interests of management *vis-a-vis* those of shareholders as a class).<sup>141</sup> As a result of the significant capital concentration across the region,<sup>142</sup> controlling shareholders are enabled to extract private benefits of control. If this situation remains unharnessed, non-controlling shareholders may be expropriated.<sup>143</sup> Consequently,

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141. For a detailed discussion on agency problems, *see* KRAAKMAN ET AL., *supra* note 6.

142. *See* GORGA, *supra* note 26 and accompanying text. It is noteworthy that the capital structure seen in the Latin American region, is somewhat similar to that of Continental Europe. Thus, in terms of agency problems, the solutions proposed in both regions should share certain characteristics. Klaus J. Hopt notes:

In Continental European company laws, the primary principal-agent conflict is not so much the conflict between shareholders and the board of directors, but rather the conflict between minority shareholders and the majority shareholder. This reflects the different prevailing patterns of stock ownership and control structures in the United States and Great Britain on the one hand and, broadly speaking, in Continental European states on the other.

*See* Hopt, *supra* note 7, at 1166.

143. Commenting on the several notions of corporate governance, Donald Clarke notes the following regarding protection of minority shareholders:

This concept is concerned with issues of finance and agency cost and has a policy component: the prevention of the exploitation of those who supply the money by those who control it. It centers on the relationship between stockholders, the board of directors, and senior management, and in effect asks, with Schleifer and Vishny, '[H]ow can financiers be sure that, once they sink their funds [into a firm], they get anything but a worthless piece of paper back from the manager?'

the Model Law contains provisions designed to counteract potential abuse of rights.<sup>144</sup> This theory of abuse of rights has been widely developed in foreign jurisdictions, particularly when dealing with the exercise of voting rights by majority shareholders.<sup>145</sup> The institution of abuse of rights (*abus de droit*) has become an important mechanism for protecting shareholders in close corporations in countries adhering to the civil law tradition, which generally lack the equity remedies present in the common law.

Article 42 of the Model Law states that “[s]hareholders shall exercise their voting rights in the interest of the simplified stock corporation.”<sup>146</sup> In this vein, when there is evidence of decisions rendered by a corporate body undertaken for the sole benefit of controlling shareholders, or aimed at purposes different from the corporate interest, the affected parties may seek judicial redress. Motives that constitute abuse of right may include inflicting harm or damages upon other shareholders or the corporation, or unduly extracting private gains for personal benefit, among others.

The abuse of rights theory is applied to three different instances, depending on the facts of the case: abuse of majority, abuse of minority and abuse of equal shareholdings (i.e., dual ownership on a fifty-fifty distribution). By adopting these protection mechanisms, the provisions of the Model Law introduce to Latin American Corporate Law the important developments on this field, spearheaded by French courts. Barthélémy Mercadal has noted on this regard that:

Voting rights may not be used in a discretionary manner. Courts will often temper voting liberty through the application of the abuse of right doctrine. Thus, they will penalize any and all decisions responding to an abusive exercise of voting rights, i.e., those votes issued in contradiction to the corporation and cast with the sole purpose of benefitting the majority (or minority) shareholders to the detriment of their

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*See* Clarke, *supra* note 18, at 79.

144. *See* Model Law, *supra* note 1, at art. 42.

145. In the United States, the language used is that of “oppression” instead of abuse. *See* Matter of Kemp & Beatley, Inc. 473 N.E.2d 1173 (N.Y. 1984).

146. *See* Model Law, *supra* note 1, at art. 42.

counterparties.<sup>147</sup>

The action for abuse-of-right provided under the Model Law may result in damages and rescission of an abusive act.

#### *H. Restructuring Transactions*

The rules on restructuring transactions in the Model Law are more flexible as compared to traditional corporate law prevailing in the Latin American region. For instance, Article 33 of the model act includes the so-called “short form merger.” This transaction may take place within a corporate group and consists of a merger of a subsidiary entity into its parent. In order for this transaction to proceed, it is necessary that the parent entity of the simplified corporation shall own at least 90 percent of the outstanding shares of its subsidiary. In this event, the latter can be merged with the former, after a decision taken by the directors or managers of both entities. The short-form merger is an exception to the general rule whereby the shareholders meeting is the only corporate body entitled to make decisions regarding structural changes.<sup>148</sup>

The Model Law also contains a specific provision concerning the sale of all or substantially all assets of the corporation.<sup>149</sup> In this type of transaction, the selling entity may receive either cash or shares of the purchasing entity as consideration. The Model Law defines it as the event where “a simplified stock corporation purports to sell or convey assets and liabilities amounting to 60% or more of its equity value . . . .”<sup>150</sup> In this event, the selling corporation does not cease to exist immediately, as is the case in a merger transaction. In fact, in order for it to be extinguished, it is necessary to wind up the corporation through the distribution of its remaining assets. The sale of all or substantially all assets, which obviously takes place

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147. BARTHELEMY MERCADAL, *MEMENTO PRATIQUE : SOCIETES COMMERCIALES*, 584 (Éditions Francis Lefebvre 1995).

148. The short-form merger was first introduced by Anglo-American company law. DEL. CODE ANN. (Delaware Code Annotated) tit. 8, § 253, contains the relevant provisions. For a detailed discussion, see REYES, *supra* note 10, at 132.

149. See Model Law, *supra* note 1, at art. 32.

150. *Id.*

outside of the ordinary course of business, requires majority shareholder approval.

Additional provisions are included to protect the rights of minority shareholders in restructuring transactions of simplified corporations, including the applicability of dissenter rights and appraisal remedies under certain circumstances.<sup>151</sup>

### *I. Dissolution and Winding Up*

It is as important to consider the legal framework for the formalization of business entities, as the rules relating to their dissolution and winding up. Therefore, it is useful to thoroughly regulate the entire cycle of a business, so that it can be formalized at the outset in accordance with up-to-date legal provisions and also be able to close its operations and resolve all relations with creditors and shareholders at the end of such a cycle. This is particularly relevant in light of the obvious fact that many of the business entities will not be successful and therefore will need to close their operations and resolve all outstanding legal situations before extinction. In that sense, it is useful to provide a few suggested rules to govern its dissolution and liquidation.

The Model Law contains three articles devoted to the dissolution and winding up of the simplified corporation. These rules are particularly useful for corporations that have gone out of business but need not resort to an insolvency proceeding to close their operations and resolve all situations with creditors and shareholders. This situation frequently takes place in MSMEs in cases in which the corporation's liabilities do not exceed the value of available assets after dissolution. In these situations, it is necessary for those responsible for the business venture to provide publicity concerning the state of liquidation, appoint liquidators, prepare inventories and other financial statements, sell corporate assets, pay liabilities according to legal priorities, and eventually return any remaining assets to the shareholders.

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151. *Id.* at art. 30.

Article 34 of the Model Law contains the events of dissolution. There is an attempt in the Model Law to simplify the processes of dissolution and liquidation in order to make them expeditious, less ritualistic, and more in tune with contemporary business needs. Dissolution for the simplified corporation will become effective as of the date at which the shareholders' decision to wind up the business entity, or the acknowledgment of the relevant legal cause for dissolution, is filed before the commercial registry. There is no need for further proceedings or decisions rendered by any third party. The only exception to the above mentioned rule relates to such cases in which the term of duration has elapsed (if expressly included by the shareholders in the company's by-laws). In this case, the corporation will be dissolved automatically.

Furthermore, dissolution does not take place in events related exclusively to the reduction of a minimum number of shareholders, or the increase of shareholders above a predefined number. The absence of provisions setting forth plurality requirements or caps concerning the amount of shareholders effectively excludes any mandatory winding up events resulting from such circumstances.

Article 35 of the Model Law contains provisions aimed at curing the events of dissolution. The inclusion of these methods responds to the fact that, whenever materially possible, it is deemed to be less costly to preserve the business, instead of allowing for its dissolution. Consequently, the Model Law establishes that dissolution events may be cured by adopting any and all measures available to that effect, provided that such measures are adopted within one year, following the date in which the shareholders' assembly acknowledged the cause of dissolution.<sup>152</sup> Furthermore, in order to incentivize the conversion of other business entities into simplified corporations, and with the aim of furthering corporate law beyond the present state of formalism, the Model Law contains an additional provision intended to avoid dissolution.<sup>153</sup> In fact, whenever there is a

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152. See Model Law, *supra* note 1, at art. 35.

153. *Id.*

business entity, organized under any form for which an event of dissolution consists of the reduction of the minimum number of shareholders, partners or members, such instance may be cured by conversion into a simplified corporation. Article 35 of the Model Law mandates that in order for this event to take place, a unanimous decision must be rendered by the holders of all issued shares, or by the will of the surviving shareholder, partner or member.

### *J. Dispute Resolution*

According to comparative legal theory, the adoption or transplantation of substantive rules of a foreign origin may have a limited impact on the receiving jurisdiction, if the transplanted rules are not adequately accompanied by an effective institutional framework aimed at facilitating their enforcement.<sup>154</sup> Consequently, the Model Law contains provisions concerning dispute resolution mechanisms, which are oriented towards the efficient application of the law in the event of disputes among business parties.

The rules on this topic include the well-known methods of arbitration and mediation. The adoption of these mechanisms responds to the frequent lack of expeditious judicial enforcement mechanisms throughout the region.<sup>155</sup> The Model Law also contains an additional

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154. See Mendoza, *supra* note 30:

The imposition of foreign rules without concern for local conditions (i.e. demand for law, pre-existing political and social arrangements, institutional background) is usually a recipe for failed legal transplants. Under this view, the principal effect of the program mentioned earlier was to increase the disparity between the law in the books and the law in action without significant improvements in the actual protection of outside investors.

Katharina Pistor further illustrates the point: “Without ensuring complementarities between the new law and preexisting legal institutions, harmonization may distort rather than improve the domestic legal framework.” Katharina Pistor, *The Standardization of Law and Its Effect on Developing Economies*, 50 AM. J. COMP. L. 98 (2002).

155. For example, under the Chilean law on simplified corporations, arbitration is mandatory in all instances. This effectively bars parties from taking disputes related to or under the simplified corporation, to state judges. See art. 441 Cód. Com. (Chile), as modified by Law no. 20190, June 5, 2007. Although this solution may seem drastic, it is merely a natural response to the dramatic situation of judicial backwardness experienced throughout the region.

dispute resolution system, which relates to the assignment of adjudication powers to specialized judicial or quasi-judicial courts. This proposal is intended to counteract the general absence in Latin America of specialized judicial tribunals in charge of commercial or corporate law matters.

The Colombian experience in this regard is noteworthy. In this jurisdiction, a short-term solution to the lack of specialized courts has been the introduction of a quasi-judicial decision making body within a governmental entity (i.e., Superintendence of Companies). This type of court has been in place in that country during the last five years. Such experiment has proven to be highly successful.

The technical quality of specialized corporate law judges has been recognized as a crucial factor for the development of corporate law.<sup>156</sup> It is obvious that having well trained, expert adjudicators results in better decisions. In the Colombian case, the Superintendence has a higher level of technical qualification and, consequently, a better understanding of complex corporate issues, as compared to the ordinary judges. Furthermore, the degree of predictability, legal certainty, and expeditiousness of this specialized court is much higher than that of the regular judiciary. This point will be dealt with in more detail in Section V below.

Article 39 of the Model Law also limits the possibility of appealing the first instance decisions rendered by this specialized tribunal. This is an attempt to curtail the common practice of endlessly appealing processes to higher judicial instances. This will produce greater legal certainty as litigating parties will avoid being subject to protracted litigation.<sup>157</sup> The additional safeguards for litigants in Latin America, such as appeals for the violation of due process can be achieved through writs of constitutionality that are commonplace in Latin America (*amparo*, *tutela*, and *mandado de segurança*).

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156. See Enriques, *supra* note 84. See additionally REYES, *supra* note 10, at 147: "The underlying rationale for bypassing ordinary courts has to do with the notion that cases should be heard by highly-qualified officials with specialized technical and professional knowledge of corporate law."

157. See Model Law, *supra* note 1, at art. 39.

## IV. EMPIRICAL DATA ON SIMPLIFIED CORPORATIONS IN COLOMBIA

As stated above, the OAS Model Law on simplified corporations is altogether based upon the Colombian Law 1258 of 2008 by means of which the SAS was introduced in that country.<sup>158</sup> The Colombian simplified corporation has proven to be effective and useful for local and foreign investors. The empirically tested effects of the Colombian legislation provide a compelling argument which favors the adoption of the Model Law. The Colombian simplified corporation (SAS) has been in existence for almost a decade, with an unprecedented success and an equally unparalleled impact in the business community.<sup>159</sup> The OECD recently acknowledged the positive effect of recent legal reforms in the country, including legislation aimed at streamlining procedures for starting a business: “Over the last decade Colombia has significantly improved its regulatory environment by simplifying the process to start a business, paying taxes, protecting investors and resolving insolvency, as well as reducing entry costs and barriers to entrepreneurs.”<sup>160</sup> Simplification procedures to start a business are, to a large extent, a result of the adoption of the SAS’ enabling regulation.

In simple terms, the Colombian SAS is by far the most successful business vehicle created in the country. Alongside the wide recognition of its benefits by the local business community, reputed legal scholars have acknowledged the success of this Colombian legal experiment: “[T]rue success stories may be mentioned from the

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158. In its recommendations to the OAS on the proposed Model Act on Simplified Stock Corporations, Dr. David P. Stewart highlighted the fact that such Model Law is based on the Colombian law from the outset. He said the following: “At our March 2011 regular session, the Chair proposed that the Committee should consider the topic of a ‘simplified stock corporation,’ with particular reference to the new law adopted by the Congress of the Republic of Colombia in December 2008.” Stewart, *supra* note 16, at 1.

159. The Colombian reform is partly based on the French SAS (Société par Actions Simplifiée), which was initially introduced in the mid 1990’s and has been updated since. See, among many others, Conac, *supra* note 46.

160. *Economic Survey of Colombia 2017*, OECD, at <https://perma.cc/V2MX-MUHT>.

viewpoint of creation of new corporate structures. One of such instances is the introduction of the simplified joint stock corporation, whose initial adoption by French Law, has been continued, by Colombian Law, with an even more positive response by business practice.”<sup>161</sup> Likewise, Professor Pierre Henri Conac has stated that: “Its success has been so great that this type of entity has replaced all other forms of business associations existing in the country.”<sup>162</sup>

Since the introduction of the Colombian simplified corporation in 2008, the country has experienced a certain degree of “competition” among different types of business vehicles.<sup>163</sup> Over the course of the years, the SAS phenomenon gave rise to a reduction in the use of other corporate forms which existed prior to its creation. The less sophisticated legal devices in pre-SAS company law may even render the future use of traditional business corporate entities unnecessary.<sup>164</sup> The SAS has received wide recognition as the most convenient vehicle to conduct business, given its simplified nature and the low level of transaction costs

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161. Embid, *supra* note 74, at 48.

162. Conac, *supra* note 46, at 30.

163. Although Latin America has no competing market for corporate chartering due to the non-existing harmonization of private law, the EU has long since benefited from such a process. Recently, describing the prevailing trends in Germany and the positive impact of importation of different models, it has been noted that: “This situation [of competition for corporate chartering] has given rise to the importation, into Germany, of numerous companies with a more flexible structure than that of the *GmbH*, but with similar functions. Notably, the English *company limited by shares*, known commonly as the *Ltd.*” Miguel Gimeno Ribes, *Un modelo societario de éxito en el Derecho alemán*, in *SOCIEDADES MERCANTILES*, *supra* note 25, at 337.

164. It has been argued that:

The SAS has displaced all traditional business forms that existed during the 1971 Colombian Commercial Code rule. Today these outdated forms represent less than 4% of the total amount of business entities that file articles of association before the country’s 52 Mercantile Registries. Not surprisingly, the remaining 96,6% of the new incorporations corresponds to the formation of new Simplified Corporations. This is probably due to the formalistic nature of the previous regulation and the SAS’ reduced transaction costs, simplified structure and contractual flexibility. Moreover, the new type of entity has sparked legal innovation and fostered new business structures that were difficult to design in the recent past, given the rigidities of the Commercial Code regulation.

Reyes, *supra* note 33, at 2.

associated with its formation and operation.<sup>165</sup> This assertion is evident in light of the exponential growth of the simplified corporation in Colombia, during the last decade, as discussed below.

*A. Number of SAS Created Since the Enactment of Law 1258 of 2008*

The Colombian SAS Law 1258 was enacted on December 5, 2008. Within 25 days after such enactment, 160 of these entities had been created, representing 7.42 percent of the total number of entities registered in December of such year. By the end of 2009, the SAS was already the prevailing type of corporate entity being created in Colombia. As seen in the Table below, during January of that year, 293 simplified corporations were formed, which corresponded to 11 percent of the total amount of business entities created in that month. By December of 2009, 1,551 SAS were incorporated. This figure raised the percentage of the total amount of business entities created in that month to 74.2 percent. As of December 2009, the traditional business association forms in Colombia, i.e., the *sociedad anónima* (regular corporation), the *sociedad colectiva* (general partnership), the *sociedad en comandita* (limited partnership), and the *sociedad de responsabilidad limitada* (closely held corporation), represented only 25.8 percent of the total business incorporated in that period.

**Table 4.** Number of SAS Incorporated in 2009<sup>166</sup>

Month	Number of SAS incorporated	Percentage out of total
January	293	11%

165. According to Albán, *supra*, note 25, at 174 n. 5, José Miguel Embid introduces the idea of a “simplification spectrum,” whereby different jurisdictions may be placed according to the contractual freedom awarded to businesspersons. In the words of José Miguel Embid, as cited by Jorge Oviedo Albán, Colombia would be placed in the “maximum” freedom category “due to the wide reception of contractual freedom, which has been introduced by the simplified model, alongside the repertoire of traditional figures.”

166. Source: *Confederación de Cámara de Comercio, CONFECÁMARAS*, at <https://perma.cc/Y2ZC-WVB3>.

Month	Number of SAS incorporated	Percentage out of total
February	629	19,8%
March	1019	33,8%
April	1184	39,4%
May	1424	47,6%
June	1544	53,6%
July	2052	59,4%
August	1773	62,4%
September	2316	66,5%
October	2183	67,8%
November	1872	70,2%
December	1551	74,2%

In 2010 the number of SAS continued to rise. During that year, more than 70 percent of the entities registered on a monthly basis were of this type. This fact provides evidence as to the progressive shrinking of traditional business forms predating SAS regulation.

**Table 5.** Number of SAS Created in 2010, and Percentage Out of the Total Entities<sup>167</sup>

Month	SAS entities registered	Percentage out of total
January	2,422	70%
February	3,091	71%
March	3,364	74%
April	2,817	74%
May	2,879	77%
June	3,069	79%
July	2,923	78%
August	3,448	81%

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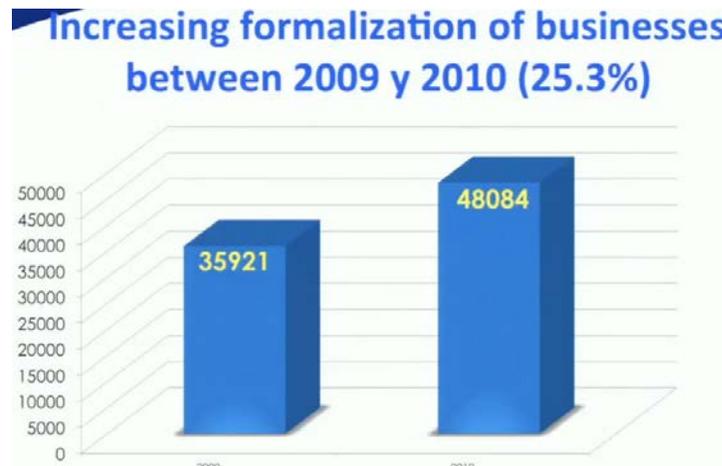
167. *Id.*

<b>Month</b>	<b>SAS entities registered</b>	<b>Percentage out of total</b>
September	3,734	82%
October	3,414	83%
November	3,275	84%
December	2,935	82%

These data show the rapid adoption of the SAS, and suggest that the Colombian business community was in dire need of a corporate vehicle which was flexible enough to accommodate their needs.

#### *B. Formalization and the SAS*

A comparative measurement concerning the rate of formalization of business shows that the number of units formalized went from 35,921 in 2009 to 48,084 in 2010. This data show an impressive 25.3 percent increase in the formalization of business entities in a single year. It is evident that the flexibility afforded by the SAS regulation is responsible for the significant number of businesses that migrated from the informal sector to full formality. An increase of more than one quarter in the number of formal incorporations is an eloquent demonstration of the potential of SAS to improve the business capacity of developing countries. As already explained, formalization also improves compliance with labor and social security regulations, enhances publicity and transparency, and may increase the amount of taxes collected by the Government.

**Figure 6.** Formalization of Business Units from 2009 to 2010<sup>168</sup>

### C. Dimension of Incorporated SAS

Aside from the impact of SAS on formalization, it is noteworthy that this type of corporate vehicle is useful for all types of undertakings, both in terms of business activity and dimension. The Colombian SAS has not only been useful for thousands of MSMEs, but also appropriate for large business undertakings. The data in Table 5 below show a substantial number of business ventures that have chosen the SAS to carry out their economic activities. The broad majority of MSMEs are created as simplified corporations.

**Table 6.** Newly Created Business Entities in Terms of Size<sup>169</sup>

Size	Employees	Total Assets <sup>170</sup>	2009	2010	2011	2012	2013	2014	2015	2016
Micro	1-10	< 501	86,362	84,776	81,744	77,954	75,679	62,229	56,262	60,570
Small	11-50	501-5,000	443	1,736	4,095	7,060	8,508	8,275	5,753	3,966
Medium	51-200	5,001-30,000	46	279	849	1,484	2,097	1,397	947	590
Large	> 200	> 30,000	10	52	173	363	577	312	242	113

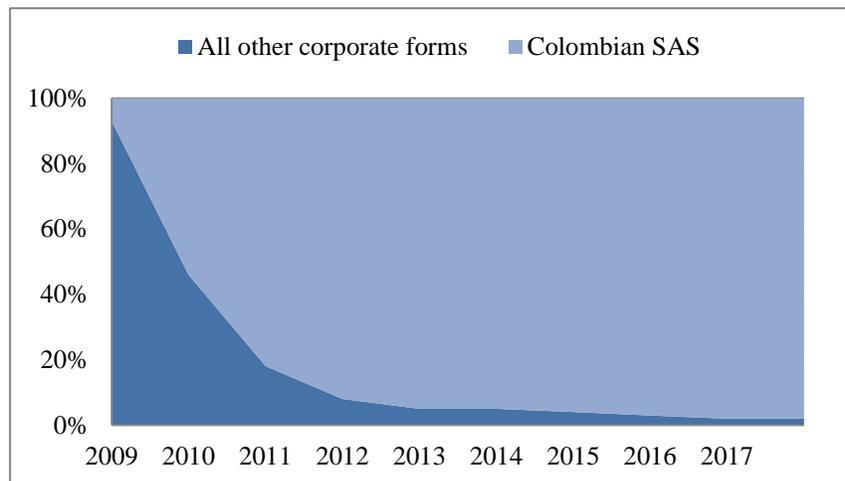
168. *Id.*

170. Calculated in Colombian minimum monthly wages (*Salario mínimo legal mensual vigente*). One minimum monthly wage is equivalent to USD 251,728 (at an exchange rate of COP 2,930 for USD 1).

#### D. SAS Versus Traditional Business Associations

As already noted, the menu of traditional business entities existing before the SAS was not responsive to market needs. As a consequence, the new technology incorporated in the simplified corporation's legislation has resulted in a significant migration to the more suitable framework of the SAS. Figure 7 and Table 7 show the outstanding progress made by this company type *vis-à-vis* the previously existing ones. In less than a decade, the Colombian SAS has come to represent almost the whole market share of new registered entities, with 98 percent of businesses created as such by the end of 2016. Figure 7 evidences the rapid growth and superiority of the SAS, while Table 7 presents detailed figures which show the actual amount of registered entities for each year beginning in 2009.

**Figure 7.** Growing Market Share of SAS in Colombia<sup>171</sup>



170. Calculated in Colombian minimum monthly wages (*Salario mínimo legal mensual vigente*). One minimum monthly wage is equivalent to USD 251,728 (at an exchange rate of COP 2,930 for USD 1).

171. See *Confederación de Cámara de Comercio*, *supra* note 166.

**Table 7.** Detailed Market Share of SAS in Colombia<sup>172</sup>

Year	Total Registered Corporations <sup>173</sup>	Total SAS Registered <sup>174</sup>	Percentage
2009	40,690	21,809	54%
2010	47,356	38,725	82%
2011	58,676	53,713	92%
2012	62,685	59,239	95%
2013	63,861	60,975	95%
2014	72,213	69,578	96%
2015	63,205	61,315	97%
2016	65,240	63,710	98%
2017 <sup>175</sup>	33,815	33,139	98%

The success of the Colombian SAS can be attributed to this entity's superior *production technology*. As it has already been stated, its simple configuration allows for an easy adaptation to the businessperson's specific needs. Colombian entrepreneurs quickly realized the potential present in the SAS as contained in its forward looking legislation. Additionally, greater formalization of MSMEs has been achieved due to the fact that transaction costs have been reduced and the SAS law has allowed for a single shareholder to incorporate as a separate and distinct legal entity.

Following the Colombian experience reflected in the data presented above, one can only expect that the widespread adoption of the Model Law in other Latin American countries would likely produce similar effects. These results could arguably ensue, in spite of the absence of a harmonized private law regime in this region.

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172. *Id.*

173. This includes all types of business forms other than the SAS, namely: the *sociedad anonima* (regular corporation), the *sociedad colectiva* (general partnership), the *sociedad en comandita* (limited partnership), and the *sociedad de responsabilidad limitada* (closely held corporation).

174. Including newly formed entities and corporations already in existence, transformed into SAS.

175. Data between January 1st and May 31st, 2017.

## V. SPECIALIZED CORPORATE DISPUTES COURT

The Colombian experiment concerning the simplified corporation also included the creation of a specialized corporate law court designed to be a sophisticated forum for the adjudication of corporate disputes. The longstanding experience of the Colombian Superintendence of Companies was a critical element in order for this new jurisdiction to be implemented.<sup>176</sup>

The Superintendence of Companies<sup>177</sup> has had limited and exceptional quasi-judicial powers since 1971. This entity is in charge of a special adjudication mechanism which is in line with the principles of the 1991 Colombian Constitution.<sup>178</sup> Nevertheless, only by 2008 did the entity form a specialized corporate law court, which

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176. In order to address the issue properly, it is necessary to review first the legal and social conditions, which prompted the legislator to establish this mechanism:

Pursuant to comparative law analytical principles, it is advisable to study the specific economic, social and political realities that underlie any given institution. Failing to do so may result in misleading conclusions vis-à-vis a particular legal reality. In the case of Latin American corporate law, such a reality is one of discrepancy between the law in the texts and its actual application.

REYES, *supra* note 10, at 40.

177. The Colombian Superintendence of Companies is a governmental entity entrusted with supervision and other faculties over companies in the country. In the words of Robert Charles Means:

The *Superintendencia* [Superintendence] possesses a broad mandate to supervise the creation and operation of Colombian non-financial corporations. The enactment of Law 58 of 1931 by which the Superintendence was initially created was permeated by the idea of protection concerning the interests of shareholders and other stakeholders from potential abuses carried out in business corporations.

MEANS, *supra* note 88, at 283. The official comment written by the Congressmen who prepared the draft legislation establishing the entity reads as follows: "The disrespect of the corporate entity in our system is paradigmatic. We all have numerous examples taken from real life to prove that it is a threat against a person's equity to contribute assets to a corporation. This word is tantamount to loss, failure and fraud." See REYES, *supra* note 132, at 625.

178. The Colombian Commercial Code [C. COM], issued under Decree 410 of 1971, introduced the first quasi-judicial functions to the Superintendence of Companies in the sphere of insolvency proceedings. As these functions were consolidated with time, and the positive results secured the mechanism, the legislator gradually increased the matters to be decided by the entity. Additionally, article 113 of the 1991 Colombian Constitution (CONSTITUCIÓN POLÍTICA DE COLOMBIA) mandates that the executive branch of government can undertake certain limited judicial functions of a non-criminal nature.

was radically updated in 2012 under a new and more efficient framework model. This adjudicating body is entrusted with deciding over a broad range of corporate disputes.<sup>179</sup>

The technical prowess of the Superintendence of Companies, with over 87 years of experience in the supervision of companies, should also be noted. This track record ensures a deep understanding of the corporate law issues which are brought before this forum:

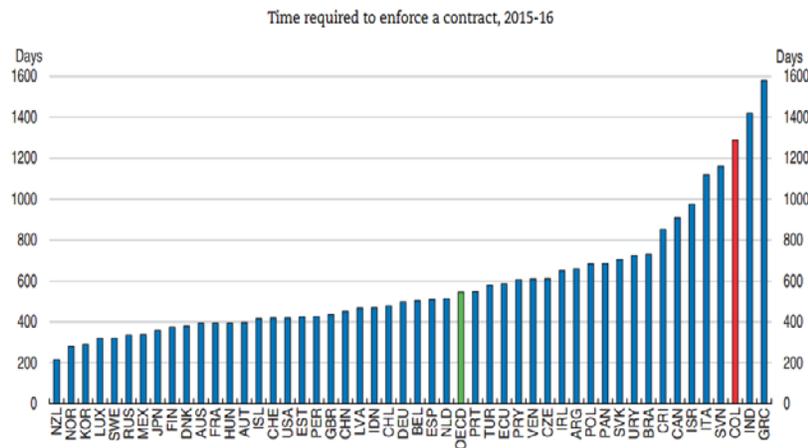
[O]ne of the Superintendence's major contributions to the interstitial development of Colombian corporate law relates to the 'administrative jurisprudence' that it has provided. In fact, reported 'precedents', doctrinal opinions and no-action letters form an impressive body of law that is permanently used as a point of reference to elucidate the meaning of corporate law provisions. Such reporting of decisions and other relevant materials supplies a large degree of predictability as to the outcome of proceedings that are litigated before the Superintendence. Robert Charles Means recognized this fact when he asserted that the Superintendence's 'primary contribution to the development of Colombian corporate law has been through its jurisprudence.'<sup>180</sup>

The Colombian experience demonstrates that, although not a strictly orthodox solution, this dispute resolution mechanism by a governmental entity, adequately responds to local problems with the judiciary. First and foremost, among these problems is the pathological judicial delay, as evidenced in Figure 8 below, which shows that Colombia ranks almost in last place when measuring the number of days required to enforce a simple debt contract, far behind OECD standards. Therefore, one of the primary objectives of conferring quasi-judicial functions to an administrative agency has been to redress the judicial backlog in rendering decisions. As will be shown below, one of the main aspects in which the specialized court stands out concerns its expeditious handling of cases.

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179. Originally, the law provided only for adjudicating disputes over SAS companies, but gradually the legislature has extended the procedures to cover all types of corporate vehicles.

180. Reyes, *supra* note 122, at 52.

**Figure 8.** Number of Days Required to Enforce a Contract<sup>181</sup>

Source: World Bank, Doing Business Database, 2017.

### A. Matters Brought to the Colombian Specialized Corporate Law Court

Since the adoption of the SAS law in Colombia, the Superintendence of Companies has consolidated over time as a very relevant Corporate Law court in Latin America. Law 1564 of 2012 by which the Colombian Code of Civil Procedure was adopted, provides broad adjudicating functions to the above mentioned Superintendence, regardless of the corporate form within which the dispute arises (excluding financial entities under the surveillance of the Financial Superintendence). The substantive matters to be adjudicated by the Superintendence of Companies are as follows<sup>182</sup>:

1. Lifting the corporate veil;

181. OECD, *supra* note 13, at 73. The OECD study has noted that: Companies regularly rely on the court system to enforce contracts or settle disputes. Lengthy and cumbersome procedures of dealing with courts can substantially add to firms' costs and reduce their productivity. Enforcing a standard debt contract takes much more time than in OECD and EMEs . . . . [H]igher enforcement costs hamper firm productivity, and this effect becomes particularly pronounced for young firms . . . .

*Id.*

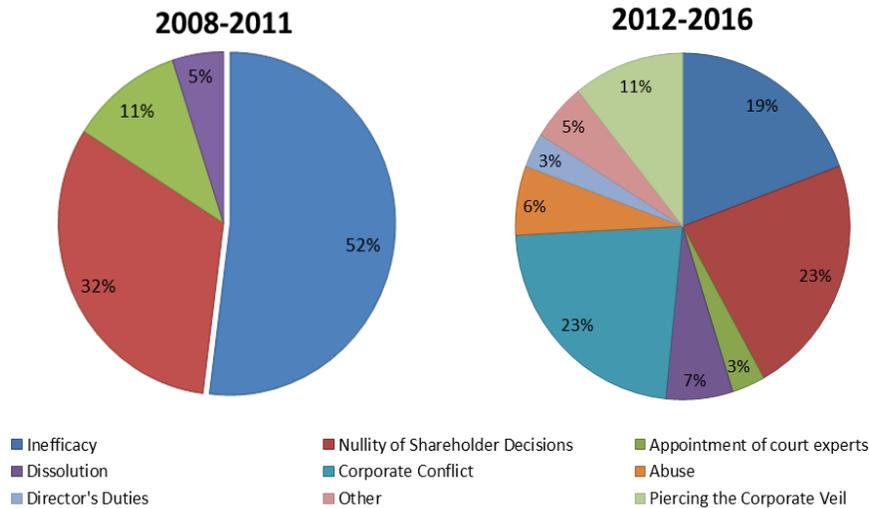
182. As contained in CÓDIGO DE PROCEDIMIENTO CIVIL (Civil Procedure Code) art. 24.5 [C.P.C]; articles 133, 136 and 148 of Law 446 of 1998; and articles 28, 29 and 43 of Law 1429 of 2010.

2. Compliance with and specific performance of undertakings within a shareholders agreement;
3. Actions intended to set aside decisions rendered by corporate bodies (i.e., shareholders' assemblies and boards of directors);
4. Acknowledgement of situations resulting in nullification;
5. Appointment of experts;
6. Discrepancies over the occurrence of situations resulting in dissolution;
7. Adjudication of intra-corporate conflicts;
8. Abuse of voting rights;
9. Liability of managers and directors; and
10. Opposition to corporate reactivation.

Some of these actions are entirely new for the Colombian legal system, and thus constitute an innovation in terms of protection mechanisms for businesspersons. As shown in Chart 1 below, it is relevant to observe that from 2008 and 2011, the complaints filed before this court related exclusively to four different issues ((i) appeals of previous corporate decisions; (ii) intra-corporate disputes; (iii) actions to set aside resolutions of the shareholders meeting; and (iv) requests for dissolution). Alternatively, as of 2012, the types of legal disputes were significantly broadened to encompass additional matters (including, *inter alia*, (i) processes for lifting the corporate veil; (ii) the appointment of experts to provide appraisals of shares of stock, and (iii) actions arising from the abuse of rights).

As an example of the above, causes of action for corporate abuse were introduced by both the SAS' law and by the procedural reforms of 2012. The innovation present in the new protections awarded for corporate abuse has dramatically increased legal certainty in Colombia, given the high degree of predictability and the introduction by the new court of a precise language establishing the situations which give rise to judicial remedies. This increased scope of matters that are resolved at the specialized corporate court is starting to provide credibility to the government's ability to enforce substantive law provisions contained in the legislation.

**Chart 1.** Corporate Law Matters Brought Before Specialized Court<sup>183</sup>



### *B. Broad Access to the Specialized Court*

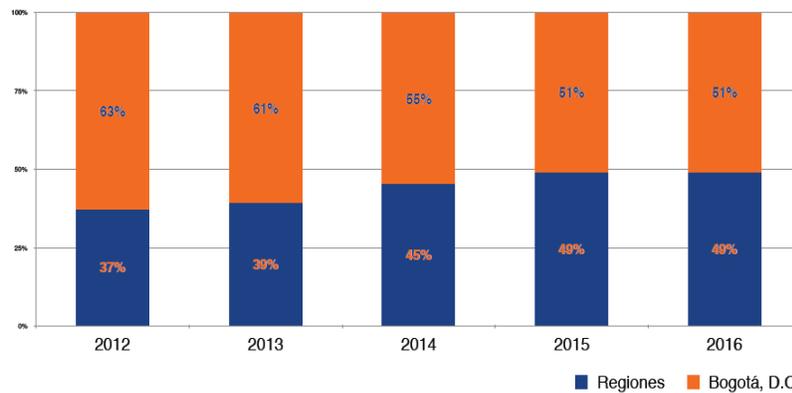
The specialized court has made use of technology, ever since its inception, in order to facilitate public access to justice. Colombia is a highly centralized Republic, thus, parties located outside of the main capitals could not seek judicial redress or enforcement of contracts in Corporate Law related matters. Since 2012, live internet streaming has been used by the court to carry out proceedings with the participation of litigants and businesspersons located in remote regions of the country. As shown in Figure 9 below, almost half of the lawsuits are currently filed electronically from locations away from the country's capital. This means that swift and effective justice is reaching areas where there was none before. The already analyzed trend which has taken place from 2012 to 2016 has not been restricted to Bogotá. In fact, there is an increasing participation of litigators from several different regions.

Additionally, the Superintendence of Companies has introduced

183. Source: SUPERINTENDENCIA DE SOCIEDADES, at <https://perma.cc/V3PM-LRE8>.

an electronic submissions platform, which allows users to present their briefs and get notified online, and facilitates communication between the judge and the clerks. This mechanism means that all proceedings may now be carried out electronically, without the need for parties to travel to the country's capital city in order to either initiate action or defend themselves before the judge.

**Figure 9.** Percentage of Lawsuits Filed in Bogotá “vis-à-vis” other Regions<sup>184</sup>

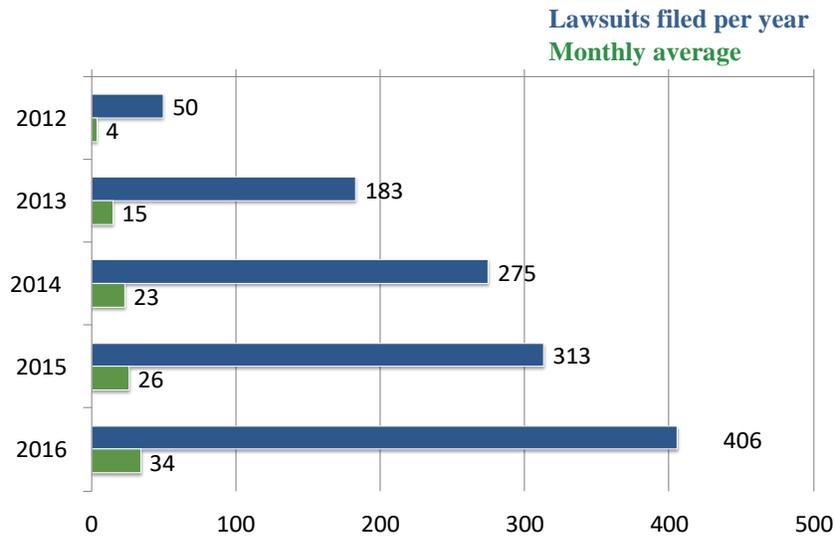


### C. Productivity and Performance of the Specialized Court

The performance of the specialized court is also noteworthy. Figure 10 below presents the total number of lawsuits filed since 2012. The steady increase in the use of the court evidences the growing confidence that businesspersons and their advisors have in the adjudication organism. In 2012, there was an average of only 4 lawsuits per month. This amount has since risen steadily up to 34 lawsuits per month by the end of 2016. This effectively means that from 2012 to 2016, the Superintendence of Companies has dealt with 1,227 corporate lawsuits.

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184. *Id.*

**Figure 10.** Corporate Law Related Lawsuits 2012-2016<sup>185</sup>

The growing confidence of businesspersons in the specialized court, evidenced by the growing number of lawsuits brought, is very likely due to the fact that the Superintendence has been able to benefit from the insights of corporate law expert judges, highly trained clerks, and appropriate physical and technological facilities which allow for an adequate adjudicating environment. This is added to the experience and insight on corporate law matters gained by the Superintendence within its functions as the companies' supervisor agency.

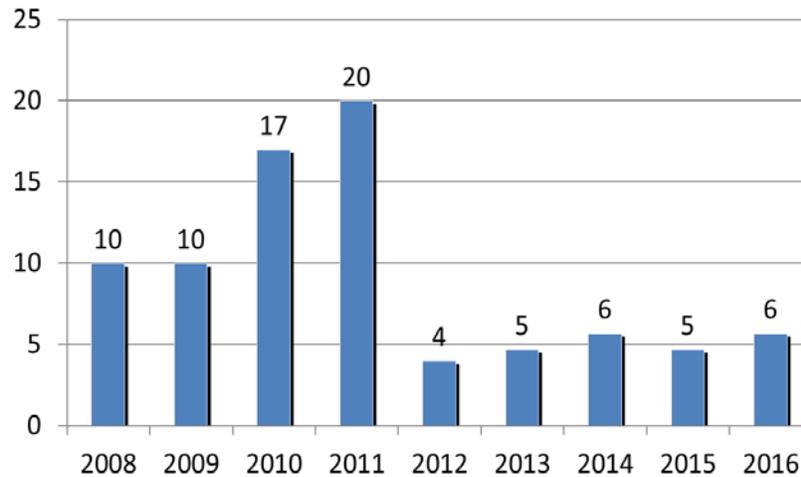
Another key aspect of the specialized court is its ability to decide cases expeditiously. In a country accustomed to protracted litigation, endless formalities, and corruption in the judicial system, it is a great achievement to have a jurisdiction in which these vices are absent. The high quality of the decisions rendered by the specialized corporate court and the short time required to obtain a final judgment speak eloquently for the great success of this legal experiment. Figure 11 below shows the efficient operation of the new jurisdiction in terms of the average time employed by the court to render a final

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185. *Id.*

decision. This reduces the heavy burden of transaction costs for litigating parties. In 2011, before the introduction of the specialized court, adjudication of such disputes lasted approximately 20 months. However, after 2012, the specialized court has reduced this time period to an average of about six-months. This is the amount of time effectively taken to decide the case, from the moment in which the complaint is notified, until the final decision is rendered.

**Figure 11.** Duration of Proceedings in the Specialized Court (months)<sup>186</sup>



## VI. CONCLUSION

The Model Law on simplified corporations for Latin America constitutes a breakthrough on several levels. The initiative promotes a harmonized legal framework tailor-made to the emerging economies of the region. The initiative's primary objective is to generate economic growth for the jurisdictions which adopt the model legislation by enabling businesspersons to incorporate with ease and migrate to the formal economy.

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186. *Id.*

The Model Law takes into consideration some of the prevailing difficulties present in the different company laws and corrects them by introducing a forward looking and simplified legal framework. The Model Law's provisions are also crafted to strike a balance between common law and civil law elements in order to find creative and purposeful solutions. This characteristic establishes a useful symbiosis which is based on the region's specific characteristics and thus caters to its particular development needs.

The Model Law also has a proven track record, based on the success of the Colombian experience with the SAS. Consequently, the initiative benefits from the real life experiment carried out during almost a decade in one of the region's jurisdictions. This ensures that the solutions provided by the Model Law constitute a proven formula for the advancement of the economies in transition.

