VOTING AGREEMENTS IN ARGENTINA: IS IT POSSIBLE TO INVEST WITHOUT UNNECESSARY RISKS?

RODRIGO S. LUCHINSKY

REVISTA ELECTRÓNICA DE DERECHO SOCIETARIO, Nº5, MAYO DE 2001(WWW.SOCIETARIO.COM)

A large number of foreign investors looking to acquire equity holdings in Argentine companies wonder whether they can be adversely affected by voting agreements (VA) that they had no knowledge of and, also, whether the voting agreements (*pacto de sindicación de acciones*) executed by them may ultimately be revoked by in a court action. These questions lead us to examine some unclear and obscure issues stemming from the current Argentine regulations governing corporations (*sociedad anónima*) and the public offering of securities.

The expression "voting agreements" is used in Argentina and in Latin America in general to refer to the event where some (or occasionally all) of the holders of shares of a corporation (or of the interest-holders of other company types[1]) execute an agreement[2] governed by the requirements of the parties and of the law, whereby each of the parties is bound to vote his shares in a certain manner[3]. Legal scholars agree that the legal nature of these agreements is similar to the legal nature of companies. However, in VAs there are no revenues, or contributions to a common fund, or a legal capacity that is different from the legal capacity of the subscribers. All such characteristics are typical of Argentine corporations.

Before the current companies law was passed, Argentine jurists were in disagreement as to whether voting agreements were legally valid. A large number of scholars was of the opinion that they were not valid because such agreements limited the power of each holder to freely vote his shares, and distorted the true nature of shareholder meetings, which were created to act as a sort of "parliament house" where the shareholders discussed issues

---

[1] Under Argentine law, persons holding interests in companies other than corporations (*sociedad anónima*) may also execute VAs. VAs are also often executed by members of Limited Liability Companies (*Sociedades de Responsabilidad Limitada*). In this paper, however, I will only focus on voting agreements in corporations because under Argentine law only corporations are allowed to publicly offer their equity securities.
[2] VAs may be either written or oral.
[3] See Luchinsky, Rodrigo and Luchinsky, Rubén, "Sindicación de Acciones", Doctrina Societaria N°150, May 2000, Editorial Errepar.

affecting the life of the company [4]. However, many local scholars took a more pragmatic, forward-looking view of the matter and suggested that voting agreements were valid and that they were to be governed by Civil Code contract regulations.

The Companies Act (Law No. 19,550 of April 25, 1972), a federal law, failed to include VAs in its regulations. The drafters of the Act were of the opinion that VAs were "para-corporate" agreements, i.e., agreements that fell out of the purview of the Companies Act[5]. Consequently, the decision as to whether VAs were valid or not rested with the courts, which were to decide on the basis of general rules and regulations on the matter. At the time, number of countries in continental Europe[6] had also approached the issue in the same manner. The Companies Act did not provide a direct solution to the problem, although it contained no provisions banning the execution of voting agreements. Additionally, the legal scholars drafting the Act had stated that the validity of voting agreements was governed by the principles of civil and commercial law. This paved the way for both legal scholars and courts[7] accepting the validity[8] of voting agreements.

In this context, a shareholder who executes a voting agreement will be bound by its terms just like he would if he had entered into any other contract. Only the parties executing the agreement will be bound by it[9]. Voting agreements are not enforceable against the corporation. In other words, if the person charged with performing the actions (trustee, another shareholder or any other person) set forth in the agreement fails to perform, a shareholder resolution that did not take into consideration the terms of the VA may not be challenged using the remedies provided in the Companies Act (Law No. 19,550). An action against the person who failed to fulfill his duties under the agreement may be commenced and damages may be claimed on the basis of such person's nonperformance.

---

[4] See footnote number 4.
[5] "A number of institutions have advocated that regulations on the validity of voting agreements be included in the Act. This Commission decided not to include such regulations for a number of reasons: a) these agreements or arrangements do not fall within the purview of a companies act. Although they may affect the corporation, these agreements are foreign to it. They are "para-corporate" arrangements that do not bind the corporation and that may be challenged by the corporation if they distort or affect its actual business". Preliminary Recitals, Law No. 19,550, Chapter II, Section 5.8.10., December 28, 1971.
[6] Italy, Spain and France, among others.
[7] See "Sánchez, Carlos c/ Banco de Avellaneda y otros", September 22, 1982, National Court of Appeals in Commercial Matters, Panel "C".
[8] See footnote number 6.
[9] This is known as the "effects of an agreement between the parties" and arises from Civil Code Article 503: "Obligations only have effects with respect to the obligee and obligor and to their transferee successors and assigns"

In light of the above, a person executing a VA together with other shareholders has to be aware of the fact that, upon nonperformance, he will not be able to sue the corporation or request that the shareholder resolution be annulled. The issue will be treated as if it were a mere case of contract nonperformance.

The other issue that needs to be examined is that there are virtually no regulations governing the disclosure of voting agreements. Since VAs were not included in the Companies Act, the law does not require that VAs be disclosed or that they be recorded in a private or government registration office. The lack of regulation has two negative effects. Firstly, since the corporation is not legally bound by the voting agreement (the corporation is merely a third party that is not contractually bound by it) a person executing an VA cannot know for sure whether the corporation will observe the agreement, especially in light of the fact that disclosure of the agreement to the corporation is not required. Secondly, shareholders not participating in the VA or investors who would like to become shareholders will never know for sure whether the other shareholders have executed an VA that may adversely affect the interests of such investors or non-participating shareholders.

Actually, in the Argentine legal system there is a set of rules that govern the disclosure of VAs, but such set of rules is limited and inefficient. The Argentine Securities Commission (*Comisión Nacional de Valores*) (CNV)[10], an institution akin to the Securities and Exchange Commission in the US[11], passed General Resolution 290 on July 22, 1997. The Resolution established a new set of disclosure rules for publicly traded companies that publicly offer their equity securities. Resolution 290, Chapter 17 (Public Offering Transparency Regulations), provides that the managing officers and the members of the control bodies of securities issuers under public offering regulations are required to report to the CNV any significant event that may materially affect the market trading, price, volume or placement of equity securities. Article 3 provides that "knowledge of the existence of voting agreements" on the part of such officers or members constitutes a significant event that must be disclosed. The Securities Markets Act (*Ley de Bolsas y Mercados de Valores*) of July 22, 1968 (Federal Law No. 17,811) sets forth the procedure to be followed if CNV regulations are not complied with. The Act also describes the penalties and court remedies available.

[10] Created by Federal Law No 17,811 of July 22, 1968.
[11] Created by Section 4 of the Securities Exchange Act 1934.

However, I am of the opinion that these provisions are useless, and there are a number of reasons for this. First, only the managing officers and members of the control body of the company –and not the shareholders who executed the VA– are required to disclose the VAs. The legal obligation to disclose a voting agreement exists only if one of the parties to it is a managing officer or control body member. Second, General Resolution 290 requires that VAs be disclosed by officers or members who have "*knowledge* of the existence of voting agreements" (emphasis added). In other words, no legal obligation arises if a managing officer states that he has no knowledge of the existence of a VA. Although it is possible to furnish evidence to the contrary, i.e., showing that the officer or member had in fact knowledge of the VA, it is extremely difficult to produce it, so much so that no cases where such evidence was produced have been recorded so far. Third, even if a VA were disclosed to the CNV, there is no system in place to publicize the disclosure. The accuracy of the information and the expediency with which such information is released to the public will greatly depend on the stock market where the company's securities are registered at. Lastly, even if an appropriate disclosure regulatory framework were in force, the CNV lacks enforcement resources given the number of companies publicly offering their securities. The situations described above create additional risk factors for investors seeking to acquire equity holdings in Argentine companies. In today's globalized world there is an overt competition between securities markets. Consequently, an unclear investment-related legal framework adversely affects local economies. However, I am convinced that we do not need countless resources to change that situation. Some legal scholars favor amending the Companies Act (Law No. 19,550) and the regulations governing the public offering of securities (Law No. 17,811 and CMV General Resolution 290/97) to make it obligatory for the parties to VAs to disclose such agreements and to make them enforceable against the securities issuing company. Other jurists suggest that the problem could be solved if the CNV were given more comprehensive investigative powers and financial resources, as well as the possibility of imposing higher penalties on violators. I am of the opinion that both solutions should be furthered. On the one hand, effective VA disclosure regulations should be implemented so that shareholders and investors alike can have knowledge of existing voting agreements. On the other hand, we need to give the CNV better enforcement tools (i.e., wider investigative powers and more financial resources).

Clearly, the benefits of streamlining the regulations governing voting agreements – thus bringing greater capital market transparency – exceed the costs of the reforms suggested in this paper. All it takes is the necessary political will.