2012

Why Do Shareholder Derivative Suits Remain Rare in Continental Europe?

Martin Gelter
Fordham University School of Law, mgelter@law.fordham.edu

WHY DO SHAREHOLDER DERIVATIVE SUITS REMAIN RARE IN CONTINENTAL EUROPE?

Martin Gelter[*]

INTRODUCTION 844
1. THE BASICS 846
1.1. The Significance of Derivative Suits 846
1.2. The Tradeoff between Enforcement and Abuse 849
1.3. Continental European Models of Derivative Litigation . 853
2. THE ANNA KARENINA PRINCIPLE: EXPLANATIONS FOR THE ABSENCE OF SUITS 856
2.1. Minimum Share Ownership Requirements 856
2.2. Costs and the Allocation of Litigation Risk 861
2.2.1. Law Firm Driven Litigation in the U.S. 861
2.2.2. The "Loser Pays" Principle 862
2.2.3. No Contingency Fees 866
2.2.4. Requirement to Advance Court Fees 869
2.3. Access to Information 870
2.4. Limitations Regarding Potential Defendants 875
3. THE PATH OF LEAST RESISTANCE: DO WE NEED DERIVATIVE LITIGATION? 881
3.1. Rescission Suits 881
3.2. Criminal Investigations 887

---

* Associate Professor, Fordham Law School, and Research Associate, European Corporate Governance Institute. For helpful comments, I thank Pierre-Henri Conac, Luca Enriques, Francesca Giannoni-Crystal, Kristoffel Grechenig, Federico Mucciarelli, Mathias Siems, the participants of the Fordham Law Alumni Association European Chapter meeting that took place at LUISS Guido Carli University, Rome, Italy, in July 2011, and the participants of the October 2011 Symposium on the Globalization of the US Litigation Model at the Dennis J. Block Center for the Study of International Business Law at Brooklyn Law School.

3.3. The Dutch Inquiry Proceedings 889
CONCLUSION 891

> *"Happy families are all alike; every unhappy family is unhappy in its own way."*
>
> LEO TOLSTOY, ANNA KARENINA (1878)

INTRODUCTION

The objective of this symposium piece is to explore why shareholder derivative suits are rare in Continental Europe. I mainly focus on Germany, France, and Italy, and further provide less extensive references regarding derivative suits in Austria, Belgium, the Netherlands, Spain, and Switzerland. In doing so, I compare the Continental European situation with the one in the United States and Japan, where derivative suits are important mechanisms of corporate governance enforcement. It is sometimes thought that shareholder litigation and litigiousness in general are cultural features of U.S. society.[1] In Japan—where shareholder derivative suits have also become common since the early 1990s—cultural theories gave way to theories emphasizing economic incentives that were more strongly supported by the evidence, as no discernible cultural shift occurred when suits became widespread.[2] I also emphasize economic incentives set by the legal framework to explain the scarcity of derivative suits in Continental Europe. This explanation, similar to the explanation provided for Japan, is also only cultural as far as legal and structural constraints setting these incentives are part of the respective culture. The two points I seek to make are summarized under the headings of the "Anna Karenina Principle" and "The Path of Least Resistance."

1. *See, e.g.*, Scott H. Mollett, *Derivative Lawsuits Outside of Their Cultural Context: The Divergent Examples of Japan and Italy*, 43 U.S.F. L. REV. 635, 654 (2009); Mathias M. Siems, *Private Enforcement of Directors' Duties: Derivative Actions as a Global Phenomenon*, *in* COLLECTIVE ACTIONS: ENHANCING ACCESS TO JUSTICE AND RECONCILING MULTILAYER INTERESTS? 4 (Stefan Wrbka, Steven Van Uytsel & Mathias Siems eds., forthcoming 2012), *available at* http://ssrn.com/abstract=1699353 (both discussing cultural explanations of derivative litigation).

2. Mark D. West, *The Pricing of Shareholder Derivative Actions in Japan and the United States*, 88 NW. U. L. REV. 1436, 1439–41 (1994) [hereinafter West, *Pricing Shareholder Derivative Actions in Japan & U.S.*] (criticizing cultural explanations).

In his Pulitzer Prize-winning book *Guns, Germs and Steel*, geographer and biologist Jared Diamond popularized the "Anna Karenina Principle" based on the first line of Leo Tolstoy's classic novel. Tolstoy suggested that happy families share a number of core characteristics that must all be present to ensure happy family life. Diamond varies the idea to explain that an animal species needs to meet a list of criteria, including diet, social behavior, and breeding habits, to be susceptible to domestication by humans.[3] The relatively small number of domesticable species can thus be explained by the observation that if even one criterion on the list is not met, the species would be too onerous to employ for human purposes. Likewise, only the United States and Japan seem to "get it right" with respect to all necessary criteria to make derivative litigation a successful model for shareholders. By contrast, no single factor suffices to account for the scarcity of derivative litigation in Continental Europe—or even a single country. I survey the available and some additional explanations, and suggest that several criteria have to be met to make derivative suits attractive.

The small number of derivative suits in Continental Europe is often seen as a reason why corporate law is considered underenforced in these jurisdictions.[4] While I do not attempt to disprove this claim, I suggest that there is a significant degree of enforcement through channels of corporate law, beyond enforcement derived from derivative suits. If a legal system discourages derivative suits, disgruntled shareholders will take the "Path of Least Resistance," and resort to other enforcement mechanisms. I, therefore, address other ways in which shareholders of European corporations can seek judicial recourse that do not take the shape of derivative litigation. While this does not imply that there is the same quality and quantity of enforcement in Europe as in the United States, we can identify at least a limited range of partial functional equivalents.

The article proceeds as follows: Part 1 begins by discussing the basics: Part 1.1 defines the scope of the investigation and establishes some comparative fundamentals. While European legal systems distinguish between two legal forms, namely the public company[5] and the private

3. JARED DIAMOND, GUNS, GERMS AND STEEL 157–75 (1997).

4. *E.g.*, Gérard Hertig, *Western Europe's Corporate Governance Dilemma*, *in* CORPORATIONS, CAPITAL MARKETS, AND BUSINESS IN THE LAW 265, 280 (Theodor Baums, Klaus J. Hopt & Norbert Horn eds., 2000).

5. This includes the German, Austrian, and Swiss *Aktiengesellschaft*; the French, Swiss, and Belgian *société anonyme*; the Italian *società per azioni*; the Spanish *sociedad anónima*; and the Dutch and Belgian *Naamloze vennootschap.* A firm incorporated as a

company,[6] I discuss only the former (derivative suits tend to be easier in the latter category). Section 1.2 describes the general issue all corporate law systems have to deal with, namely the tradeoff between effective enforcement of corporate law and prevention of abusive lawsuits that are used to divert resources to plaintiffs. Part 1.3 gives a brief overview of the various European models of shareholder litigation. Part 2 discusses possible reasons for the absence of derivative suits in Continental Europe. Some of the arguments have been discussed frequently, such as minimum ownership thresholds and the distribution of litigation risk through litigation cost rules. Others have received less or no attention, such as limits to the information available to defendants, and limits to who can be sued derivatively. Part 3 suggests that the absence of derivative suits may not be as detrimental as one might think at first glance by showing that derivative litigation is not the only possible avenue for private corporate law enforcement. Without attempting to provide a complete picture, I look at three Continental European enforcement models, as follows: Part 3.1 investigates rescission (nullification) suits, which are common in several countries, but subject to a particularly intense debate in Germany, where it is often argued that they can be abused by "predatory shareholders"; 3.2 discusses criminal enforcement under French law, on which shareholders are able to "piggyback"; and 3.3 looks at the Dutch model, where derivative suits are not available and the unique "inquiry proceedings" are the chosen method for resolution of many corporate conflicts of interest. The larger theoretical point is that shareholders will seek the "path of least resistance" in litigation. If derivative litigation does not provide a good option, maybe another legal mechanism (such as the ones described in Part 3) will. Finally, the Conclusion summarizes and concludes.

1. THE BASICS

1.1. The Significance of Derivative Suits

Robert Clark emphasizes that the American derivative suit was originally conceived as a combination of two suits: "The plaintiff (1) brought

---

public company does not necessarily have to be publicly traded (the majority of firms are not).

6. The German, Austrian, and Swiss *Gesellschaft mit beschränkter Haftung*; the French, Swiss, and Belgian *société à responsabilité limitée*; the Italian *società a responsabilità limitata*; the Spanish *Sociedad de responsabilidad limitada*; and the Dutch and Belgian *Besloten vennootschap* are therefore not discussed, as well as newer "hybrid" forms such as the French *société par actions simplifiée.*

a suit in equity against the corporation seeking an order compelling it (2) to bring a suit for damages or other relief against some third person."[7] Derivative suits were—and are—typically brought against directors or officers of the corporation.[8] While litigation on behalf of the corporation is normally one of the tasks within the wide range of the board's powers,[9] the board is unlikely to bring a suit against one of its members or against an officer, whom the board appointed and who works under the board's supervision.[10] Against this conflict of interests, the derivative suit provides a safety valve by allowing shareholders to push the corporation into litigation.[11] Much of Delaware case law revolves around the circumstances under which directors can avoid a suit. Even when shareholders have good intentions and their claims are likely to succeed, these suits may not be in the best interest of the corporation.[12]

There is strong evidence that the number of derivative suits in the United States is quite large, however, the suits are outnumbered by shareholder class actions—which are brought for *personal* claims of all shareholders[13]—and by securities class actions. For example, Thompson and Thomas report that, in 1998 and 1999, 824 class actions, 87 individual direct actions, and 137 derivative actions were brought in Delaware based on alleged violations of fiduciary duty.[14] Nevertheless, the niche for derivative actions remains sizeable.[15]

---

7. ROBERT C. CLARK, CORPORATE LAW 639 (1987); *see* Aronson v. Lewis, 473 A.2d 805, 811 (Del. 1984).

8. Anne Tucker Nees, *Who's the Boss? Unmasking Oversight Liability within the Corporate Power Puzzle*, 35 DEL. J. CORP. L. 199, 214 n.56 (2010).

9. *See* DEL. CODE ANN. tit. 8, § 141(a) (2011).

10. *See* Kenneth B. Davis, Jr., *The Forgotten Derivative Suit*, 61 VAND. L. REV. 387, 397 (2008); Agostino v. Hicks, 845 A.2d 1110, 1116 (Del. Ch. 2004) ("[D]irectors and officers of a corporation may not hold themselves accountable to the corporation for their own wrongdoing.").

11. *See* Zapata Corp. v. Maldonado, 430 A.2d 779, 782 (Del. 1981); Taormina v. Taormina Corp., 78 A.2d 473, 475 (Del. Ch. 1951) ("[T]he action is brought as a class action . . . on behalf of all other stockholders of the Corporation similarly situated.").

12. *See, e.g.*, *Maldonado*, 430 A.2d at 779–85.

13. Delaware uses the Tooley test to distinguish between derivative and direct suits (which include class actions) on the basis of whether (1) the corporation or shareholders allegedly suffered harm, and (2) who would receive the benefit of the remedy. Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031 (Del. 2004).

14. *E.g.*, Robert B. Thompson & Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133, 168–69 (2004).

15. As shown by Mark West, Japan is the one country that seems to have adopted the U.S. practice of the derivative suit on a large scale. Mark D. West, *Why Shareholders*

The European evidence is fragmentary, but commentators that discuss individual countries uniformly confirm that the number of suits is very low.[16] In the United Kingdom, an investigation by Armour et al., spanning 2004 through 2006, brought to light only twenty-six suits in which directors were named as the defendants.[17] I am not aware of any systematic evidence for Continental Europe. Cheffins and Black report only two suits against German supervisory board members before 1997 in which

---

Sue: The Evidence from Japan, 30 J. LEGAL STUD. 351, 351 (2001) [hereinafter West, *Why Shareholders Sue*].

16. *E.g.*, Kristoffel Grechenig & Michael Sekyra, *No derivative shareholder suits in Europe: A model of percentage limits and collusion*, 31 INT'L REV. L. & ECON. 16, 16 (2011) (suggesting a general absence of derivative litigation in Europe). For specific countries, see, for example, Lukas Glanzmann, *Die Verantwortlichkeitsklage unter Corporate-Governance-Aspekten* [*The Liability Action under Corporate Governance Aspects*], 119 ZEITSCHRIFT FÜR SCHWEIZERISCHES RECHT [ZSR] 137, 174–75 (2000) (Switz.) (noting the small significance of shareholder litigation in Switzerland); YVES GUYON, 1 DROIT DES AFFAIRES—DROIT COMMERCIAL GÉNÉRAL ET SOCIÉTÉS [BUSINESS LAW—COMMERCIAL LAW AND ASSOCIATIONS] ¶ 462 (2003) (Fr.) (stating that the "*action sociale ut singuli*" is rarely exercised); Dominique Schmidt, *De quelques règles procédurales régissant l'action en responsabilité civile contre les dirigeants de sociétés « cotées » in bonis* [*About severel procedural rules regarding the civil liability action against the directors of publicly traded companies*], *in* ÉTUDES DE DROIT PRIVÉ. MELANGES OFFERTS À PAUL DIDIER 383, 391 (Michael Germain & Jean Foyer eds., 2008) (Fr.) (noting that the number of suits in France is insignificant); Paolo Giudici, *Representative Litigation in Italian Capital Markets: Italian Derivative Suits and (if ever) Securities Class Actions*, 6 EUR. COMPANY & FIN. L. REV. 246, 249 (2009) ("[T]he Italian derivative action exists on paper, but not in the real world"); Dario Latella, *Shareholder Derivative Suits: A Comparative Analysis and the Implications of the European Shareholders' Rights Directive*, 6 EUR. COMPANY & FIN. L. REV. 307, 319 (2009) ("At present, there are no suits exerted in Italy and, therefore, no data available."); Marcus Lutter, *Zur Durchsetzung von Schadenersatzansprüchen gegen Organmitglieder* [*The Enforcement of Compensation Claims against Board Members*], *in* FESTSCHRIFT FÜR UWE H. SCHNEIDER ZUM 70. GEBURTSTAG 763, 764–65 (Ulrich Burgard, Walther Hadding, Peter O. Mülbert, Michael Nietsch & Reinhard Welter eds., 2011) (Ger.) [hereinafter FESTSCHRIFT FÜR UWE H. SCHNEIDER] (noting that neither "predatory shareholders" not plaintiffs bringing legitimate suits have appeared since the 2005 reform of shareholder litigation in Germany); Klaus Ulrich Schmolke, *Die Aktionärsklage nach § 148 AktG*, [*The Shareholder Action under § 148 AktG*], 40 ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT [ZGR] 398, 402–03 (2011) (Ger.) (explaining that there were only three relatively insignificant cases of derivative suits in Germany have been reported since the 2005 reform).

17. John Armour, Bernard Black, Brian Cheffins & Richard Nolan, *Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States*, 6 J. EMPIRICAL LEGAL STUD. 687, 699 (2009).

damages were awarded at trial.[18] Ulmer reports only two published German cases awarding damages on the basis of a submission by shareholders between 1965 and 1999.[19] Pierre-Henri Conac, Luca Enriques, and I began to compile a database of published French, German, and Italian cases decided between 2000 and 2007 where self-dealing by controlling shareholders is alleged. While this can provide us only with a limited (and maybe not even the main) subset of derivative suits, it is still interesting to note that we have so far found only two such suits in Germany (one of which related to a GmbH, roughly the equivalent of an LLC), two in Italy, and one in France.[20] There is, however, very good data on rescission suits in Germany.[21]

1.2 The Tradeoff between Enforcement and Abuse

Are the effects of shareholder litigation beneficial? Intuitively, corporate law requires an enforcement mechanism. Directors and officers who do not expect sanctions for violating duties of care, loyalty, or good faith have little reason to comply with these duties. Generally the decision to bring a lawsuit is within the competence of a corporation's directors,[22] who are unlikely to bring a lawsuit on behalf of the corporation and name themselves as defendants.[23] Without derivative suits, enforcement would be highly improbable, except after a change of the management team, e.g. because ownership of the corporation changed or because the

---

18. *See* Brian R. Cheffins & Bernard S. Black, *Outside Director Liability across Countries*, 84 TEX. L. REV. 1385, 1424 (2006).

19. Peter Ulmer, *Die Aktionärsklage als Instrument zur Kontrolle des Vorstands- und Aufsichtsratshandelns* [*The Shareholder Action as an Instrument to Control Executive and Supervisory Board Actions*], 163 ZEITSCHRIFT FÜR DAS GESAMTE HANDELS- UND WIRTSCHAFTSRECHT [ZHR] 290, 295 n.19 (1999) (Ger.).

20. In fact, in most of the cases in our database judicial recourse was not sought through a derivative suit, but in other ways. *See infra* Section 3.1.

21. *See infra* Section 3.1.

22. For France, see, for example, PHILIPPE MERLE & ANNE FAUCHON, DROIT COMMERCIAL. SOCIÉTÉS COMMERCIALES [COMMERCIAL LAW: BUSINESS ASSOCIATIONS] ¶ 409 (13th ed. 2009) (Fr.); for Germany, see UWE HÜFFER, AKTIENGESETZ [STOCK CORPORATION ACT] § 147, ¶ 1 (9th ed. 2010) (Ger.) (explaining that normally the management board and supervisory board act on behalf of the company).

On shareholders' power to pass a binding resolution to litigation, *see infra* note 50 and accompanying text. In Spain and Belgium, the law simply states that the shareholder meeting decides about liability suits, apparently without explicitly providing for a suit to be brought by directors. *See* LEY DE SOCIEDADES ANÓNIMAS art. 134.1 (B.O.E. 1989, 1564) (Spain); CODE DES SOCIÉTÉS [COMPANY CODE] art. 561 (Belg.).

23. *E.g.*, Arad Reisberg, *Funding Derivative Actions: A Re-Examination of Costs and Fees as Incentives to Commence Litigation*, 4 J. CORP. L. STUD. 345, 367 (2004).

old board was forced to resign after a scandal or the company's insolvency.[24] Boards of directors are typically not inclined to sue officers of the corporation, even if the officers are not members of the board.

The same holds in two-tier board models such as the German model. Under German law, the supervisory board represents the corporation vis-à-vis members of the management board.[25] While the separation of the two boards is intended to avoid conflicts of interest resulting from an overlap between the management and oversight functions, lawsuits against incumbent boards are still not frequent. The obvious reasons are that the supervisory board is also responsible for the appointment of management board members,[26] and that supervisory directors at least appear to be indirectly responsible for decisions of the management organ they are expected to monitor.[27] Decisions that give rise to litigation are, therefore, likely to shed a bad light on the supervisory board and may even lead to liability for poor oversight.[28] The same applies when the potential defendant is a supervisory board member, in which case management, representing the company, is equally unlikely to bite the hand that feeds it.[29] Interlocking directorates and inevitable social relationships between directors further widen the enforcement gap.[30]

---

24. *See* Giudici, *supra* note 16, at 248–49 (recounting that liability against directors was largely unheard of outside of insolvency before Italy introduced derivative suits in 1998); Michel Germain, *Les droits des minoritaires (droit français des sociétés)* [*Minority Rights (French Company Law)*], 54 REVUE INTERNATIONALE DE DROIT COMPARÉ [RIDC] [INTERNATIONAL JOURNAL OF COMPARATIVE LAW] 401, 409 (2002) (Fr.) (pointing out that liability suits are usually only brought after a change at the helm).

25. *See* Aktiengesetz [AktG] [Stock Corporation Act], Sept. 6, 1965, BUNDESGESETZBLATT, TEIL I [BGBL. I] at 1089, last amended by Gesetz [G], Dec. 22, 2011, BGBL. I at 3044, § 112 (Ger.). Regarding representation in the case of litigation against members of the management board, see, for example, Mathias Habersack, *in* 2 MÜNCHENER KOMMENTAR ZUM AKTIENGESETZ [MUNICH COMMENTARY ON THE STOCK CORPORATION ACT], § 112, ¶ 17 (Wulf Goette & Mathias Habersack eds., 3d ed. 2008).

26. AktG § 84 (Ger.).

27. *See* AktG § 111(1) (Ger.); Hans C. Hirt, *The Review of the Role and Effectiveness of Non-Executive Directors: A Critical Assessment with Particular Reference to the German Two-tier Board System: Part 1*, 14 INT'L COMPANY & COM. L. REV. 245, 254 (2003) [hereinafter Hirt, *The Review of the Role and Effectiveness of Non-Executive Directors*] (describing structural interdependence of the two boards).

28. *E.g.*, HANS C. HIRT, THE ENFORCEMENT OF DIRECTORS' DUTIES IN BRITAIN AND GERMANY 274–75 (2004).

29. *See* Hans C. Hirt, *The Enforcement of Directors' Duties pursuant to the Aktiengesetz: Present Law and Reform in Germany: Part 1*, 16 INT'L COMPANY & COMM. L. REV. 179, 185 (2005) [hereinafter Hirt, *The Enforcement of Directors' Duties*].

30. *See* Hirt, *The Review of the Role and Effectiveness of Non-Executive Directors*, *supra* note 27, at 253–54; Susanne Kalss, *Shareholder Suits: Common Problems, Differ-*

Shareholder derivative litigation is one possible way of filling this gap. The individual shareholder's incentive to sue, however, is weak. A potential plaintiff will only benefit from a successful suit in proportion to his share in the company, while the remaining benefits accrue to other shareholders. The plaintiff has to bear the time investment of dealing with a suit and possibly the cost. Derivative suits are, therefore, often said to produce a public good, the production of which may need to be subsidized if derivative suits are thought to have beneficial effects.[31]

Shareholder litigation, however, may not always be in the interest of the corporation or shareholders as a group. Even if there is a possible basis for liability, the likelihood of success and the potential award may be too small to make spending money and the executives' time worthwhile for the corporation.[32] Furthermore, a suit may create negative publicity that reduces sales or causes skepticism among suppliers and customers. Weighing the pros and cons against each other, the decision to litigate looks very much like other business decisions usually taken by management. Boards typically possess superior information, in comparison to shareholders, as to whether a suit would be advisable. This is why one can arguably consider the choice to bring a lawsuit a business decision—one that warrants the protection of the business judgment rule—at least as long as the decision maker is not subject to a conflict of interest. U.S. corporate law developed the "demand requirement" to strike a balance between the business judgment inherently required in the decision to litigate and conflicts of interest arising from the fact that potential defendants are directors.[33] A potential plaintiff in a derivative suit must

---

ent Solutions and First Steps towards a Possible Harmonization by Means of a European Model Code, 6 EUR. COMPANY & FIN. L. REV. 324, 336–37 (2009).

31. *E.g.*, Reisberg, *supra* note 23, at 345, 347–48 (discussing incentives to sue and free-riding); Anne van Aaken, *Shareholder Suits as Technique of Internalization and Control of Management*, 68 RABELS ZEITSCHRIFT FÜR AUSLÄNDISCHES UND INTERNATIONALES PRIVATRECHT [RABELSZ] 288, 289 (2004) (Ger.) (discussing the public good character of derivative suits).

32. *See, e.g.*, Reinier Kraakman, Hyun Park & Steven Shavell, *When are Shareholder Suits in Shareholder Interests?* 82 GEO. L.J. 1733, 1738 (1994) (discussing litigation cost). Besides these costs on the individual level, shareholder litigation may also make it more expensive for firms to hire managers. *Id.* In this case, other shareholders might react to a suit by selling.

33. *See* Brehm v. Eisner, 746 A.2d 244, 254 (Del. 2000); *see, e.g.*, DEL. CH. CT. R. 23.1 (West 2012); N.Y. BUS. CORP. LAW § 626(c) (McKinney 2003).

show that the plaintiff requested that the board of directors bring a suit or had a good reason not to do so.[34]

It is conceivable that a suit can be entirely abusive.[35] For example, a criticism that is sometimes raised in the United States is that derivative suits primarily benefit plaintiff law firms[36]—since the first shareholder bringing the suit controls the suit, law firms may engage in a race to the courthouse in order to win the prize of controlling the suit.[37] The ulterior motive of the firm, however, is to receive a contingency fee.[38] Most cases do not actually go to trial, but instead result in a settlement.[39] Under the "substantial benefits" test, plaintiff lawyers receive a contingency fee not only as a percentage of damages awarded or agreed upon as a settlement, but also on the basis of other consequences of the suit. These sometimes include corporate governance changes agreed upon with the corporation's management, such as the appointment of independent directors to the board (the financial benefits of which, if there are indeed any, are

34. *See* FED. R. CIV. P. 23.1(b)(3) and equivalent rules under state law, such as MODEL BUS. CORP. ACT § 7.42 (1984). The complaint has to "state with particularity" the efforts the plaintiff made "to obtain the desired action from the directors" or the reasons why the plaintiff failed to do so. Under Delaware law, courts will assume that by making a demand, plaintiffs concede that demand was not futile. *See* Speigel v. Buntrock, 571 A.2d 767, 775 (Del. 1990). Since directors will typically conclude that a suit is not advisable, demand is rarely made. *See* James D. Cox & Randall S. Thomas, *Common Challenges Facing Shareholder Suits in Europe and the United States*, 6 EUR. COMPANY & FIN. L. REV. 348, 352 (2009). Litigation often revolves around the disinterestedness of directors' decision not to sue. *See* Seth Aronson et al., *Shareholder Derivative Actions: From Cradle to Grave*, 1832 PLI/CORP 163, 209–14 (2010). Under the Aronson-Levine test, plaintiffs thus either have to show that the current board "could not reach a disinterested decision with respect to plaintiff's demand," or that "there was reasonable doubt about whether the board then exercised reasonable business judgment with respect to the challenged transaction." *See* Aronson v. Lewis, 473 A.2d 805, 805, 814 (Del. 1984); *Brehm*, 746 A.2d at 256.

35. *See* Mark J. Loewenstein, *Shareholder Derivative Litigation and Corporate Governance*, 24 DEL. J. CORP. L. 1, 5–6 (1999).

36. *See id.* at 2, 5–6.

37. John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 692 (1986) [hereinafter Coffee, *Understanding the Plaintiff's Attorney*].

38. *See* Jessica Erickson, *Corporate Misconduct and the Perfect Storm of Shareholder Litigation*, 84 NOTRE DAME L. REV. 75, 86 (2008); *see also* Loewenstein, *supra* note 35, at 6 (discussing the motivating force behind filing a derivative action).

39. James D. Cox, *The Social Meaning of Shareholder Suits*, 65 BROOK. L. REV. 3 (1999).

nearly impossible to measure).[40] Litigation may therefore often commence without merit and be entirely characterized by litigation agency cost.[41] The controlling law firm has an incentive to settle the case in the way not necessarily most beneficial for shareholders, but rather to maximize the firm's own benefit.[42]

But even in light of this problem, one could argue that litigation without merit in the specific case may create beneficial general deterrence. Managers and directors will have stronger incentives to shy away from anything that remotely resembles a violation of corporate law because it *could* lead to a suit, and consequently negative publicity and the hassle of legal proceedings. Contingency fees—or any other reward obtained by an "abusive" lawyer or plaintiff—could be seen as a reward needed to incentivize possible plaintiffs to monitor corporate actions. Abusive lawsuits might actually be socially valuable because only they create a sufficient deterrent effect.

1.3 Continental European Models of Derivative Litigation

Despite the general perception that derivative suits are rare in Continental Europe, they are, in principle, available in all countries surveyed here with the exception of the Netherlands.[43] (Dutch law has developed another enforcement model that will be discussed in Part 3.3.) Admittedly, some countries were relative latecomers to the concept. Belgium only introduced derivative litigation in 1991,[44] and Italy did so for listed firms only as part of a securities law reform in 1998.[45] The Italian

---

40. *See* Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 392 (1970).

41. *See* Coffee, *Understanding the Plaintiff's Attorney*, *supra* note 37, at 679–80.

42. *See In re* Revlon, Inc. S'holders Litig., 990 A.2d 940, 959 (Del. Ch. 2010); Coffee, *Understanding the Plaintiff's Attorney*, *supra* note 37, at 690.

43. STEVEN R. SCHUIT, BARBARA BIER, LEONARD G. VERBURG & JAN A. TER WISCH, CORPORATE LAW AND PRACTICE OF THE NETHERLANDS 155 (Steven R. Schuit ed., 2d ed. 2002).

44. The relevant section of the law today is CODE DES SOCIÉTÉS art. 562 (Belg.). The suit was first introduced with the *Lois coordonnées sur les sociétés commerciales* [Belgian Company Code] art. 66bis, of July 26, 1991, MONITEUR BELGE [M.B.] [Official Gazette of Belgium] (Belg.). Alexia Bertrand & Arnaud Coibion, *Shareholder Suits against the Directors of a Company, against other Shareholders and against the Company itself under Belgian Law*, 6 EUR. COMPANY & FIN. L. REV. 270, 282–83 (2009) (discussing reasons for the introduction).

45. Decreto Legislativo 24 febbraio 1998, n. 58 (It.); TESTO UNICO IN MATERIA DI INTERMEDIAZIONE FINANZIARIA [T.U.I.F.] [RULES AND REGULATIONS CONCERNING STOCK MARKET TRADING] art. 129, D. Lgs. n.58 (It.). The corporation could settle lawsuits un-

mechanism was expanded to all stock corporations—or *società per azioni*—including those that are not publicly traded, in 2003. Elsewhere, derivative suits or very close equivalents have been around for much longer. For example, France was the trailblazer and introduced the so-called *action sociale ut singuli* in 1867,[46] while Germany's slightly different minority enforcement mechanism followed suit in 1884.[47]

The litigation models of France and Switzerland, where the derivative suit is seen as an individual shareholder right and the law simply states that a corporate liability suit can be brought by a shareholder on behalf of the corporation,[48] are probably the closest to the United States' model. In Austria, Belgium, Germany, Italy, and Spain, enforcement is a collective right of shareholders that can be imposed on the corporation by a binding shareholder resolution.[49] The power of the majority is compromised by the right of a qualified minority to set litigation in motion with court approval.[50] The Belgian, Italian, and Spanish enforcement mechanisms can

---

less a minority of 5% objected in the shareholder meeting. Article 129 has been eliminated in consequence of the introduction of the derivative suit in corporate law.

46. Loi du 24 juillet 1867 sur les Sociétés [Law of July 24, 1867 on Companies], arts. 17, 39 (Fr.) (permitting a minority of 5% to bring a derivative suit). In spite of the 5% threshold, the courts soon found that this provision did not limit the individual shareholders right to bring a derivative suit; it merely set out limitations to the circumstances under which a group of shareholders could collaborate to sue jointly (in order to save cost). *See* C. HOUPIN & H. BOSVIEUX, 2 TRAITÉ GÉNÉRAL DES SOCIÉTÉS CIVILES ET COMMERCIALES ET DES ASSOCIATIONS ¶ 1431 (6th ed. 1929) (citing a list of cases beginning with Cass., 7 maie 1872, Dal. 72, I, 273 (It.)).

47. *See* Hirt, *The Enforcement of Directors' Duties*, *supra* note 29, at 184.

48. *See* CODE DE COMMERCE [C. COM.] [COMMERCIAL CODE] art. L. 225-252 (Fr.); OBLIGATIONENRECHT [OR] [CODE OF OBLIGATIONS] Mar. 30, 1911, as amended, art. 756 (Switz.). Germany follows this model only in the law of corporate groups. *See infra* notes 185–84 and accompanying text. In France, it is usually assumed that the derivative suit can only be brought if the corporation failed to sue, even though there is no formal demand requirement. *See* Hans de Wulf, *Direct shareholder suits for damages based on reflective loss*, *in* 1 FESTSCHRIFT FÜR KLAUS J. HOPT ZUM 70. GEBURTSTAG AM 24. AUGUST 2010, 1537, 1558 (Stefan Grundmann et al. eds., 2010).

49. Depending on the respective board structure, shareholders that do not fulfill the standing requirements to sue can of course alert the board, supervisory board, or board of auditors of possible wrongdoing, although this will of course not help much in many cases. *See, e.g.*, CODICE CIVILE [C.C.] art. 2393(3) (It.) (permitting the board of auditors to sue).

50. *See* C.C. arts. 2393(1), 2364(4) (It.); AktG § 147(1) (Ger.); CODE DES SOCIÉTÉS art. 561 (Belg.); AKTIENGESETZ [AKTG] [STOCK CORPORATION ACT] § 134(1) (Austria); Ley de Sociedades Anónimas art. 134.4 (B.O.E. 1989, 1564) (Spain) (providing that a minority of 5% can ask for the convocation of a shareholder meeting to decide about a liability suit, and can bring the suit if (1) the board does not convene the shareholder

be qualified as providing for actual derivative suits, even though Belgian and Italian laws require that shareholders must appoint representatives (of plaintiff shareholders).[51] The same is true for the German model introduced with the Business Integrity Act of 2005,[52] which for the first time permits a "real" derivative suit in which shareholders personally enforce a claim.[53] The old German model, which is still available as an alternative,[54] and the equivalent Austrian provisions, only create a right for a qualified minority to petition a court to appoint a special representative of the corporation to pursue liability claims against directors.[55] The

---

meeting, (2) the company does not bring a suit in spite of a decision in the shareholder meeting within a month, or (3) shareholders decide not to bring a suit).

The right to enforce claims is only one of a whole range of rights that qualified minority shareholders have in many Continental European jurisdictions. The role of minimum ownership requirements will be discussed in Part 2.1. While fiduciary duties or equivalent doctrines applying to controlling shareholders are generally recognized, I am not aware of litigation that would allege a breach for a controlling shareholders' failure to vote in favor of a liability suit. *See* Pierre-Henri Conac, Luca Enriques & Martin Gelter, *Constraining Dominant Shareholders' Self-Dealing: The Legal Framework in France, Germany, and Italy*, 4 EUR. COMPANY & FIN. L. REV. 491, 500–02 (2007).

51. CODE DES SOCIÉTÉS art. 565 (Belg.) (requiring that plaintiffs unanimously elect a representative to pursue the suit who can be a "shareholder or not"); C.C. art. 2393-bis(4) (It.) (requiring that plaintiffs elect one or more representatives by a majority vote). In Italy, shareholders also control the suit, since the law allows them to abandon or settle the claim. C.C. art. 2393-bis(6) (It.); *see* Luca Enriques & Federico M. Mucciarelli, *L'azione sociale di responsabilità da parte delle minoranze* [*Derivative Action brought by a Minority*], *in* 2 IL NUOVO DIRITTO DELLE SOCIETÀ [THE NEW CORPORATE LAW] 861, 878–79 (Pietro Abadessa & Giuseppe B. Portale eds., 2006) (It.) (criticizing that a majority shareholder could inhibit litigation by suing separately and electing a compliant representative).

52. AktG § 148 I, as amended by Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts [UMAG], Sept. 22, 2005, BGBL. I at 2802 (Ger.).

53. Regarding additional procedural hurdles, *see infra* notes 65–67 and accompanying text.

54. *See* AktG § 147(2) (Ger.).

55. Regarding the requirement to first push for the enforcement of the claim in the meeting, see UWE HÜFFER, AKTIENGESETZ [STOCK CORPORATION ACT] § 147, ¶ 4 (6th ed. 2004); Henning Schröer, *in* 4 MÜNCHENER KOMMENTAR ZUM AKTIENGESETZ § 147, ¶ 32 (Bruno Kropff & Johannes Semler eds., 2d ed. 2004) (Ger.). Before 1998, a minority of 10% or a stated capital of €1 million could request the appointment of a special representative. Gesetz zur Kontrolle und Transparenz im Unternehmensbereich [KonTraG] [Control and Transparency Act], Mar. 3, 1998, BGBL. I Nr.24 S. 786 (Ger.), reduced the ownership threshold to 5%/€500,000 for cases where petitioners were able to establish facts indicating dishonesty or serious violations of the law or the corporate charter (AktG §147 III (Ger.) (old version)) and for the first time permitted the minority right to be exercised directly without first having to go through the shareholder meeting. Shareholders could

new German framework, for the first time, gives shareholders control over the suit,[56] although the corporation can decide to take over a pending suit at any time.[57] It is also the only Continental European country to adopt the demand requirement from the United States' model.[58]

2. THE ANNA KARENINA PRINCIPLE: EXPLANATIONS FOR THE ABSENCE OF SUITS

I focus on four issues to explain the scarcity of derivative litigation in spite of its availability in principle. In analogy to the Anna Karenina principle, countries need to "get it right" in at least four dimensions to allow shareholder suits to proliferate. The four dimensions are as follows: there must be favorable standing requirements that do not include a minimum ownership threshold (Section 2.1); the litigation risk must be allocated favorably to overcome minority shareholders' rational apathy (Section 2.2); potential plaintiffs must have sufficient access to information to litigate (Section 2.3); and the enforcement model must make it possible for shareholders to derivatively sue potential wrongdoers, which not only includes directors, but also controlling shareholders (Section 2.4).

2.1 Minimum Share Ownership Requirements

A number of Continental European jurisdictions require that shareholders (or groups of shareholders) hold a qualified percentage of the company's shares or a specified amount of capital to bring a derivative suit. Percentage limits can be rationalized as a screening mechanism against abusive lawsuits on the grounds that the incentive for a shareholder with a small amount of shares to bring a legitimate suit is very likely small. Given that any shareholder's benefits from the results of a successful suit consist only of a proportionate share in the rise of the value of the corporation, it seems hard to imagine why a shareholder

---

also vote to appoint a special representative, presumably to pursue the claim more effectively. AktG § 147 II (Ger.). Currently, the appointment of a special representative can be requested by a 10% /€1 million minority.

Austrian law, which shares a historical origin with German law because of the introduction of the 1937 AktG in Austria, still provides essentially the same in AKTG § 134 (Austria).

56. Hirt, *The Enforcement of Directors' Duties*, *supra* note 29, at 188.

57. AKTG § 147(3) (Austria).

58. *See* AktG § 148(1)(2) (Ger.).

with only a few shares would sue for a legitimate reason.[59] For a small investor, a suit would seem to be rational only when the investor can somehow coerce management into an abusive settlement that constitutes an effective bribe to make the investor go away, i.e., the litigation equivalent of greenmail.[60] Theory cannot explain what particular percentage should provide the cutoff, which could be set at 1%, 5%, 10%, or any other number with almost equal justification. A plaintiff's motives are presumably legitimate when the benefits of the lawsuit, multiplied by the probability of its success, exceed the costs of litigation, including nonmonetary cost. Any percentage limit is, to some extent, arbitrary and can preclude some legitimate suits. The requirement to retain a relatively large number of shares while the suit is pending may act as a further deterrent.[61]

Grechenig and Sekyra suggest that percentage limits are to blame for the absence of derivative suits in Continental Europe.[62] Their mathematical model captures a simple intuition: in order to avoid a lawsuit, potential defendant managers only need to deal with those shareholders above the applicable threshold. In order to "bribe" these large shareholders, managers would have to offer these shareholders an advantage that exceeds their losses from managerial wrongdoing. Large shareholders, therefore, do not monitor management, but become accomplices of management in actions exploiting investors whose share is below the threshold.[63]

---

59. *E.g.*, Kalss, *supra* note 30, at 341 ("The *function* of a minimum share stake requirement is to impose part of the financial risk to be borne by the company on the claimant and, therefore, to reduce the economic motivation for suits brought for purposes of extortion."); Schmolke, *supra* note 16, at 425. The assumption implicit in this argument is that there are significant, non-reimburseable costs that do not increase in the plaintiff's share in the firm.

60. Relatedly, it is sometimes argued that small shareholders are mere investors without a long-term interest in the firm, who have no entrepreneurial interest and can express their dissatisfaction by selling his share. *See* Mathias M. Siems, *Welche Auswirkungen hat das neue Verfolgungsrecht der Aktionärsminderheit?*, 104 ZEITSCHRIFT FÜR VERGLEICHENDE RECHTSWISSENSCHAFT [ZVGLRWISS] 376, 385 (2005) (Ger.) (criticizing this argument).

61. Giudici, *supra* note 16, at 251 (discussing the Italian case).

62. *See* Grechenig & Sekyra, *supra* note 16, at 16–17.

63. *See also* Alexander Stremitzer, *Plaintiffs Exploiting Plaintiffs* 11–12 (Yale Law & Econ. Research Paper, 2010), *available at* http://ssrn.com/abstract=1085282 (reaching practically the same result under different assumptions about bargaining power between managers and minority shareholders). One could imagine that managers permit large shareholders to engage in harmful self-dealing transactions, while these shareholders will allow managers to obtain illicit private benefits. This assumption seems to be in line with

In recent years, Germany and Italy have reduced minimum ownership thresholds. The traditional German enforcement mechanism required a qualified minority of 10% or DM 2,000,000 until 1998, when it was lowered to 5% or €500,000 for cases where shareholders could establish facts indicating dishonesty or serious violations of the law or the corporate charter.[64] The derivative suit introduced in 2005 requires only 1% or €100,000.[65] To prevent abusive litigation, the German legislature introduced a special judicial "lawsuit admission procedure," or *Klagezulassungsverfahren*, during the course of which plaintiffs must show that they demanded that directors bring the suit.[66] Shareholders have to establish facts indicating dishonesty or serious violations of the law or the corporate charter, and the court must determine whether litigation would be in the interest of the company before allowing it to proceed beyond this stage.[67]

In 1998, when derivative suits were introduced, Italian law started out with a 5% threshold.[68] Since the mechanism was never used,[69] the 2003 reform eliminated the six month ownership requirement and extended it to unlisted stock corporations. In unlisted corporations, the suit is restricted to shareholders owning at least 20%, unless the corporate charter provides an even higher threshold of up to 33.3%.[70] For publicly traded

---

anecdotal evidence about financial scandals. In concentrated ownership systems, blockholders tend to be involved in wrongdoing. John C. Coffee, Jr., *A Theory of Corporate Scandals: Why the USA and Europe Differ*, 21 OX. REV. ECON. POL'Y 198 (2005). In a dispersed ownership firm where all stakes are below the threshold, there will be no suits unless shareholders are able to coordinate.

64. AktG § 147 III (Ger.) (old version). In other words, the burden of proof was more severe for smaller shareholders.

65. AktG § 148 I, as amended by UMAG (Ger.).

66. AktG § 148 II, as amended by UMAG (Ger.). Among other things, it must be shown that the firm failed to bring a suit within a reasonable period after demand was made by shareholders. A "reasonable" period seems to be about two months. *See* HÜFFER, *supra* note 22, § 148, ¶ 7.

67. To be precise, the court must determine whether there are indications that the company suffered damages from dishonesty or from serious violations of the law or the charter, and whether a suit would be contrary to the preponderating interest of the company AktG § 148 II, as amended by UMAG (Ger.). The corporation can at any time decide to pick up the suit. AktG § 148 III (Ger.).

68. Marco Ventoruzzo, *Experiments in Comparative Corporate Law: The Recent Italian Reform and the Dubious Virtues of a Market for Rules in the Absence of Effective Regulatory Competition*, 2 EUR. COMPANY & FIN. L. REV. 207, 246–47 (2005). The law also stipulated a minimum ownership period of six months. *Id.*

69. *Id.* at 247.

70. C.C. art. 2393bis(1) (It.).

firms, the threshold was reduced from 5% to 2.5% in 2006,[71] again because derivative suits failed to emerge in practice.[72]

Whereas Belgian law also only requires 1% or a nominal capital share of €1,250,000 for a derivative suit,[73] the thresholds are higher in Spain (5%)[74] and Austria (10%).[75] Table 1 provides a summary.

Country	Minimum ownership	Enforcement model	Additional notes
Austria	10%	enforcement by special representative of the corporation	5% if special audits revealed incriminating information
Belgium	1% or €1,250,000	derivative suit with mandatory shareholder representative	
France	none	derivative suit	groups of shareholders and shareholder associations need to pass thresholds to bring joint suits
Germany	1% or €100,000	derivative suit	demand requirement and judicial "admission procedure" shareholders have to establish facts indicating cases of dishonesty or serious violations of the law or the corporate charter
	10%	enforcement by special representative of the corporation	***special rules for corporate groups (see section 2.4)
Italy	2.5% (listed) or 20%	derivative suit with mandatory shareholder representative	
The Netherlands	10% or €225,000	no derivative suit, but "inquiry proceedings" (see section 3.3)	
Spain	5%	derivative suit	
Switzerland	none	derivative suit	

Table 1: Minimum ownership thresholds for minority enforcement of directors' liability in Continental European jurisdictions

71. C.C. art. 2393bis(2), as modified by Legge 28 dicembre 2005, n. 262 (It.).
72. *See* Giudici, *supra* note 16, at 250.
73. CODE DES SOCIÉTÉS art. 562 (Belg.).
74. Ley de Sociedades Anónimas art. 134(4) (B.O.E. 1989, 1564) (Spain) (referring to art. 100).
75. AKTG § 134(1) (Austria).

The percentage limit theory cannot explain the cases of France and Switzerland, where—as in the United States and Japan—individual shareholders can enforce liability claims against directors without holding a minimum stake. These laws also do not have the additional procedural hurdles of German law, such as the demand requirement and admission procedure.[76] The German situation is not well explained by the theory, since there is a special derivative mechanism available to every shareholder in the law of corporate groups, but the mechanism has also failed to produce litigation.[77] French law does not provide an ownership threshold for individual plaintiffs, but does so for groups of shareholders suing jointly[78] and for qualifying shareholder associations.[79] In these cases, the threshold amounts to at least 0.5% or 1%, respectively.[80] The collective mechanisms are preferable to the individual suit for reasons of litigation costs,[81] but the advantage is not big enough to overcome the problems set by the threshold and the lack of incentives for small shareholders to sue.

---

76. Giudici, *supra* note 16, at 252, 253 n.38. Japan also never had a threshold, and still suits appeared only in the 1990s. West, *Why Shareholders Sue*, *supra* note 15, at 352 (describing the emergence of derivative suits in Japan).

77. *See infra* Section 2.4.

78. *See* C. COM. art. L. 225-169 (Fr.). The exact threshold is computed by taking 4% of the first €750,000 of the firm's capital, 2.5% of the amount between €750,000 and €7,500,000, 1% of the amount between €7,500,000 and €15,000,000, and 0.5% for anything above that. Thus, the larger the firm's capital, the smaller the required percentage.

79. Qualifying associations can collectively exercise the certain shareholder rights, such as the convocation of the shareholder meeting, putting items on the agenda, demand the resignation of auditors, submit questions to directors, and, most interestingly for us, bring suits against directors/administrators. *See id.* art. L. 225-120, I (Fr.); ANNE CHAVÉRIAT, ALAIN COURET & BRUNO ZABALA, MÉMENTO PRATIQUE FRANCIS LEVEBVRE: SOCIÉTÉS COMMERCIALES 2010, ¶ 17903 (Francis Lefebrvre ed., 41st ed. 2009).

80. *See* C. COM. arts. L. 225-252 & L. 225-120 (Fr.). The members of a qualifying association must own a minimum number of shares depending on the firm's legal capital. *See id.* art. L. 225-120. If the firm's capital is below €750,000, the required amount is 5%; between €750,000 and €4,500,000 it is 4%, between €4,500,000 and €7,500,000 it is 3%, between €7,500,000 and €15,000,000 it is 2%, and above that it is 1%. *See id.* French law does not have a demand requirement. *See* de Wulf, *supra* note 48, at 1558.

81. Since several shareholders suing in parallel cannot delegate a member of their group as a joint representative ("nul ne plaid par procureur"), court fees are effectively multiplied by the number of suing shareholders. Groups of shareholders or shareholder associations can allows spreading cost across shareholders. *See* RAPHAËL CONTIN, LE CONTRÔLE DE LA GESTION DES SOCIÉTÉS ANONYMES ¶ 526 (1975) (Fr.); GUYON, *supra* note 16, at 496; Germain, *supra* note 24, at 409; *see also* MAURICE COZIAN, ALAIN VIANDIER & FLORENCE DEBOISSY, DROIT DES SOCIÉTÉS ¶ 619 (22d ed. 2009); MERLE & FAUCHON, *supra* note 22, ¶ 410; CHAVARÉT ET AL., *supra* note 79, ¶ 2404.

In spite of these doubts, policymakers regularly obsess about percentage thresholds.[82] Given the highly dispersed ownership structure in the United States, it is likely that even a small percentage threshold would kill most suits in publicly traded firms. It is equally unlikely that eliminating ownership thresholds would result in derivative litigation spreading across the European continent. A non-trivial ownership threshold seems to be an exclusionary criterion that will prevent the emergence of a culture of derivative litigation, but the absence of one does not guarantee its spread.

2.2. Costs and the Allocation of Litigation Risk

2.2.1. Law Firm Driven Litigation in the United States

Besides ownership thresholds, the most frequently discussed reason for the scarcity of derivative litigation is the absence of incentives to bring derivative suits.[83] In most publicly traded U.S. firms, which usually have dispersed share ownership, one would expect individual shareholders to have little, if any, incentive to sue given that they only draw a very small advantage while being burdened with a potentially substantial cost.[84] The "American Rule" in civil procedure, which requires that each party pays its own cost regardless of the outcome, could in theory deter some prospective suits that have a high probability of success.[85] Losers are only required to pay winners in rare cases where courts believe that bringing a suit was clearly abusive.[86]

The high frequency of derivative (and other shareholder) litigation is typically credited to the entrepreneurial and specialized plaintiff bar. This bar actually has quite a strong incentive to bring derivative suits given that contingency fees resulting from an award or settlement could be as high as one third of the amount.[87] Even when the settlement does not contain a monetary award, and only requires changing the firm's corporate governance practices (e.g., more independent directors), the law firm can receive a considerable award under the "substantial benefits" doc-

---

82. *See, e.g.*, Giudici, *supra* note 16, at 250 (reporting that the Italian legislator of 2006 thought that 5% was too high); Cheffins & Black, *supra* note 18, at 1425 (considering the former German 10% threshold as a reason for the absence of litigation).

83. Erickson, *supra* note 38, at 100.

84. *See id.*

85. *See* Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 391 (1970).

86. *E.g.*, Cox & Thomas, *supra* note 34, at 355.

87. *See* Erickson, *supra* note 38, at 101.

trine.[88] Specialized law firms therefore only need to find a suitable plaintiff and sometimes actually hold a stock portfolio to be able to sue once they hear about a possible claim.[89] This situation may result in a "race to the courthouse" between law firms since, traditionally, the first firm to file is assigned the role of lead counsel in the case and thus receives most of the fee.[90] However, since about the year 2000, Delaware courts have begun to rely on a variety of factors to determine lead counsel, including the size of the plaintiff's stake and the quality of the pleadings filed.[91] While this may marginally diminish suits or induce plaintiffs to take cases out of Delaware, this further illustrates that the incentive to sue rests almost entirely with the law firm.[92]

2.2.2. The "Loser Pays" Principle

European countries generally apply what in the United States is often called the "English Rule": the losing party has to reimburse the winning party for litigation costs.[93] Since the outcome of a lawsuit is rarely certain, it is often suggested that the most important factor deterring derivative suits is that shareholders will not be willing to take the risk of having

---

88. Fletcher v. A.J. Indus., Inc., 266 Cal. App. 2d 313, 320 (1968); *see also Mills*, 396 U.S. at 395–96 (noting that "an award of counsel fees, regardless of whether the benefit is pecuniary in nature" may be justified from a derivative suit where the corporation received a "substantial benefit"); Tandycrafts, Inc. v. Initio Partners, 562 A.2d 1162, 1165 (Del. 1989) (discussing the term "corporate benefit"). Note that the Delaware courts were long known to be more generous to plaintiff's attorneys than other courts, who often relied on the "lodestar" approach, which is based on the number of hours invested multiplied by the lawyer's hourly fee and adjusted by a factor depending on various characteristics of the case, like risk. *In re* Oracle Sec. Litig., 852 F. Supp. 1437, 1449 (N.D. Cal. 1994); Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 22 (1991). There is evidence that Delaware has started to act more parsimoniously recently and has hence lost market share in litigation. *See* John Armour, Bernard Black & Brian Cheffins, *Delaware's Balancing Act* 31–35 (Univ. Cambridge Legal Studies Research Paper Series, Paper No. 10-04, 2011), *available at* http://ssrn.com/abstract=1677400 (discussing attorney's fees in Delaware).

89. Coffee, *Understanding the Plaintiff's Attorney*, *supra* note 37, at 682.

90. *See id.* at 692.

91. *See* Armour et al., *supra* note 88, at 35–43.

92. *E.g.*, Coffee, *Understanding the Plaintiff's Attorney*, *supra* note 37, at 669.

93. *E.g.* ZIVILPROZESSORDNUNG [ZPO] [CODE OF CIVIL PROCEDURE], Dec. 5, 2005, BGBL I S. 3202, § 91 (Ger.); CODE DE PROCÉDURE CIVILE [C.P.C.] [CODE OF CIVIL PROCEDURE] art. 696 (Fr.); Codice di Procedura civile [C.p.c.] art. 91 (It.); SCHWEIZERISCHE ZIVILPROZESSORDNUNG [C.P.C.] [SWISS CODE OF CIVIL PROCEDURE] art. 106(1) (Switz.); ZIVILPROZESSORDNUNG [ZPO] [CODE OF CIVIL PROCEDURE] § 41(1) (Austria); CODE JUDICIAIRE [C.JUD.] § 1017 (Belg.).

to pay for the defendants' fees.[94] The argument appears persuasive at first glance. Fees often depend on the complexity of the case, which is high if it involves intricate business issues. Moreover, to the extent that fees depend on the amount in dispute, court fees will also be very high in a derivative suit given the high value at stake in such suits.[95]

From a theoretical perspective, the argument is not entirely persuasive. The obvious objection is that the effects of the English Rule cut both ways; a plaintiff not only bears the risk of having to reimburse the defendant if the suit fails, but also benefits from being reimbursed in the case of success. Thus, the rule's overall effect is to increase the dollar amount subject to litigation risk. Instead of receiving an amount between zero and the sum sought in the suit, the plaintiff's potential payoff varies from the negative amount of the defendant's cost to the sum sought plus the plaintiff's own cost. With the greater spread in possible payoffs, the effect of the English Rule is to dilute "the value of low-probability-of-prevailing cases" and enhancing "the value of high-probability-of-prevailing cases."[96] Winners' cost reimbursement favors plaintiffs who know for sure that they have a clear-cut case over those who are unlikely to prevail. The rule should, therefore, deter frivolous shareholder litigation, while encouraging meritorious suits.

Moreover, European reimbursement systems are often closer to the American Rule in practice than in theory. In several countries, including Germany and Italy, reimbursement is limited to court fees plus expenses for lawyers, according to the official tariff promulgated by the bar association.[97] Reimbursement by the loser is even more limited in France;[98]

---

94. *E.g.*, Luca Enriques, *The Comparative Anatomy of Corporate Law*, 52 AM. J. COMP. L. 1011, 1024 (2004) (reviewing REINIER KRAAKMAN ET AL., THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH (2004)) [hereinafter Enriques, *The Comparative Anatomy of Corporate Law*]; Reisberg, *supra* note 23, at 348–49 ("[T]he American treatment of fees in such actions provides significantly lower disincentives to prospective plaintiffs than does the English Rule."); Cheffins & Black, *supra* note 18, at 1425; Cox & Thomas, *supra* note 34, at 357.

95. *E.g.*, Lutter, *supra* note 16, at 765 (criticizing that a high amount in dispute may deter German shareholders from suing). Technically, the court has some discretion in setting the amount in dispute under German law. Gerichtskostengesetz [GKG] [Court Fees Act], Aug. 4, 2009, BGBL. I at 2491, § 53.

96. Kathryn E. Spier, *Litigation*, *in* 1 HANDBOOK OF LAW AND ECONOMICS 259, 301 (A. Mitchell Polinsky & Steven Shavell eds., 2007).

97. For Germany, see Martin Giebel, *in* 1 MÜNCHENER KOMMENTAR ZUR ZIVILPROZESSORDNUNG § 91, ¶ 49 (Thomas Rauscher & Peter Wax eds., 3d ed. 2008) (Ger.); ZPO § 91 II (Ger.) (first sentence). For Italy, see Giudici, *supra* note 16, at 253–54 (noting that the Italian civil procedure code applies the English rule for legal expenses). For Austria, see ZPO § 41(2) (Austria).

while court fees are usually reimbursed, lawyers' fees normally are not. These are automatically borne by the losing party only when retention of an attorney is mandatory,[99] which is generally not the case in commercial courts, where corporate cases are litigated.[100] French judges can grant lawyers' fees to the winning party under equitable considerations,[101] but, if fees are granted in practice, the amount tends to be much lower than what lawyers actually charged.[102]

Several jurisdictions have special rules regarding litigation costs for shareholder derivative suits, all of which slightly improve the position of plaintiff shareholders compared to the basic "loser pays" principle. For example, under the post-2005 German law,[103] the minority shareholder's risk is initially cabined to the cost of the special judicial procedure deciding the admission of the derivative suit. At this stage, the amount in dispute is capped at €500,000, which usually limits court fees to a four-digit figure.[104] Moreover, the corporation bears the cost if the petition is denied for reasons "in the interest of the company" about which the shareholder could not know, but which the corporation could have disclosed to the shareholder. If the petition actually proceeds to the stage of a derivative suit, the English Rule applies in principle. However, if the suit is not successful or is only partially successful, the corporation has to reim-

---

98. *See* Bernard Grelon, *Shareholders' Lawsuits against the Management of a Company and its Shareholders under French Law*, 6 EUR. COMPANY & FIN. L. REV. 205, 212 (2009) (explaining that a winning plaintiff shareholder is not fully reimbursed).

99. C.P.C. art. 696(7) (Fr.).

100. *Id.* art. 853.

101. *Id.* art. 700.

102. *E.g.*, Daniel Landry, *Les frais irrépétibles* [*The Irrecoverable Costs*], 2010 LA SEMAINE JURIDIQUE ÉDITION GÉNÉRALE [JCP-G] 1288 (Fr.); Raymond Martin, *Avocats—Obligations et prérogatives* [*Lawyers—Duties and Prerogatives*], *in* JURISCLASSEUR PROCÉDURE CIVILE 83–84, ¶ 43 (2011) (Fr.).

103. Before 2005, liability claims initiated by minority shareholders were pursued by a court-appointed special representative, who was an agent of the corporation and thus paid by it. AktG § 147 III (Ger.), before KonTraG (1998); AktG § 147 II, as amended by KonTraG (1998–2005). However, the petitioning minority shareholders had to compensate the corporation when litigation cost exceeded the award, and even had to bear court fees if the suit was entirely unsuccessful. AktG § 147 IV (Ger.) (until 2005).

104. GKG § 53 (Ger.); *see* Martin Peltzer, *Das Zulassungsverfahren nach § 148 AktG wird von der Praxis nicht angenommen! Warum? Was nun?*, *in* FESTSCHRIFT FÜR UWE H. SCHNEIDER, *supra* note 16, at 956–57 (discussing the amount of court fees); *see also* Carsten A. Paul, *Derivative Actions under English and German Corporate Law—Shareholder Participation between the Tension Filled Areas of Corporate Governance and Malicious Shareholder Interference*, 7 EUR. COMPANY & FIN. L. REV. 81, 102 (2010) (suggesting that fees hardly ever exceed €12,000).

burse the plaintiff, unless the plaintiff passed the first stage of judgment review by claiming false facts and in doing so acted intentionally or with gross negligence.[105] As a result, a good faith plaintiff should bear little risk.

In most other countries, cost rules are also slightly tweaked in favor of plaintiffs. In Italy, the corporation is not only required to pay the victorious plaintiff's litigation expenses, but also the cost of ascertaining the facts that form the basis of the suit.[106] In Switzerland and France, the court generally has the discretion to diverge from the English Rule in the case of an unsuccessful good-faith plaintiff.[107] In Belgium, the court *can* require losing shareholders to pay damages to the defendants, but *must* order the company to reimburse damages if the suit is successful.[108] In Austria, the minority can be required to pay the litigation cost incurred by the special representative only if the minority acted intentionally or with gross negligence in the pursuit of frivolous litigation.[109]

Given these theoretical doubts and the economics of the English Rule, it appears that the idea of the English Rule's deterrent power is based on the assumption that shareholder suits have a low probability of winning. If that is the case, maybe the United States only has vibrant derivative litigation because strike suits are not deterred. Moreover, the increased risk created by the English Rule may be hard to absorb for shareholder plaintiffs who tend to be worse risk-bearers than large corporations and wealthy directors with deep pockets. This issue is likely exacerbated by the reality that lawyers' fees are often not reimbursed beyond a certain basic amount, since cases with a complicated corporate fact pattern are hard to handle for non-specialized counsel. In spite of ostensively shareholder-friendly rules, often open-ended standards with respect to cost put

105. AktG § 148 VI (Ger.).

106. C.C. art. 2393-bis(5) (It.); *see also* Enriques & Mucciarelli, *supra* note 51, at 887 (pointing out that Italian law also eliminates the plaintiff's additional risk that the defendants are judgment proof and therefore cannot reimburse them).

107. C.P.C. art. 107(b) (Switz.). The official legislative report explicitly encourages judges to do so in cases of derivative suits. SCHWEIZERISCHEN EIDGENOSSENSCHAFT, BOTSCHAFT ZUR SCHWEIZERISCHEN ZIVILPROZESSORDNUNG 7297, June 28, 2006, *available at* http://www.admin.ch/ch/d/ff/2006/7221.pdf (Switz.) (mentioning the case of a small shareholder bringing a derivative suit a possible case where the court may use this discretion). Before the enactment of a uniform Swiss Code of Civil Procedure in 2009, there was an explicit rule in corporate law. OR, former art. 756(2) (Switz.). In France, the court has the same equitable power under C.P.C. art. 696 (Fr.), although this happens extremely rarely, and no specific reference to shareholder litigation is made.

108. CODE DES SOCIÉTÉS art. 567 (Belg.).

109. *See* AKTG § 135(4)–(5) (Austria).

plaintiffs at the mercy of the courts by making reimbursement uncertain. Peltzer suggests that, regarding Germany, the cost risk of an admission procedure is still too big for small shareholders, in particular when several shareholders have to coordinate to surpass the 1% threshold, in which case they are jointly and severally liable for cost.[110] In the Italian context, Giudici criticizes that the court has too much discretion in determining what costs were necessary to establish the facts and are therefore reimbursable.[111] Similar arguments can be made for other laws that rely on the plaintiff's good faith or degree of negligence to allocate litigation risk.

Overall, the purported negative effects of the loser pays principle seem to be rather an issue of how easy it is to bring a claim, specifically what burden of proof needs to be met to survive early stages of litigation or to obtain reimbursement with reasonable certainty. In order to facilitate derivative litigation, it may be more promising for European legislatures to facilitate information gathering by shareholders instead of switching to the American Rule, even if it slightly encourages more risky lawsuits.[112]

2.2.3. No Contingency Fees

Besides the "English Rule," the other classic difference that could explain the rarity of derivative suits in Europe is the absence of contingency fees. In contrast to the United States, contingency fees are uncommon and often illegal. Contingency fees have traditionally been rejected because they are thought to distort the incentives of lawyers to represent clients' interests.[113] Although the cultural aversion to a more entrepreneurial view of the legal profession may be receding, this has not yet resulted in the emergence of a plaintiff bar comparable to the American one.

---

110. Peltzer, *supra* note 104, at 956–57.

111. *See* Giudici, *supra* note 16, at 254.

112. The issue will be addressed in Section 2.3.

113. *See, e.g.*, Samuel Issacharoff & Geoffrey P. Miller, Essay, *Will Aggregate Litigation Come to Europe?*, 62 VAND. L. REV. 179, 197–99, 199 n.57 (2009) (describing resistance against derivative litigation and mentioning that England and Wales allowed conditional fees since the early 1990s); Tiffany Chieu, Note, *Class Actions in the European Union?: Importing Lessons Learned from the United States' Experience into European Community Competition Law*, 18 CARDOZO J. INT'L & COMP. L. 123, 148 (2010) ("[W]ith the exception of England and Wales, contingency fees are prohibited in EU Member States.").

Contingency fees could conceivably kindle desirable litigation, which has not eluded the attention of policymakers, scholars, and courts.[114] In France, the 1996 Marini Report on corporate law discussed the possible adoption of contingency fees in the context of class actions, but ultimately did not recommend the introduction of either instrument.[115] In Germany, the Constitutional Court declared the former blanket prohibition unconstitutional in 2006.[116] Therefore, the law regulating lawyers' fees in Germany had to be amended to permit contingency fees in restricted circumstances, specifically when a plaintiff would otherwise be prevented from pursuing the plaintiff's rights for economic reasons.[117] However, lawyers in Germany are not permitted to use contingency fees as a general strategy,[118] but only to permit indignant plaintiffs to pursue claims.[119] In July 2006, Italy took some steps towards results-based compensation for lawyers.[120] The Italian law governing lawyers' ethics now permits lawyers' fees to be made dependent on the achievement of specified goals,[121] and the former prohibition in the civil code has been elimi-

114. *See, e.g.*, Gerard Hertig & Joseph A. McCahery, *Company and Takeover Law Reform in Europe: Misguided Harmonization Efforts or Regulatory Competition?*, 4 EUR. BUS. ORG. L. REV. 179, 193 (2003) (suggesting that contingency fees could improve corporate law enforcement in the EU).

115. PHILIPPE MARINI, LA MODERNISATION DU DROIT DES SOCIÉTÉS [THE MODERNIZATION OF CORPORATE LAW] 93–94 (1996), *reprinted in* COMPARATIVE CORPORATE GOVERNANCE: ESSAYS AND MATERIALS M-113 (Klaus J. Hopt & Eddy Wymeersch eds., 1997). The legal basis for the prohibition in France is Loi 71-1130 du 31 décembre 1971 portant réforme de certaines professions judiciaires et juridiques [Reforming Certain Judicial and Legal Professorions], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], art. 10(3) (Fr.).

116. Entscheidungen des Bundesverfassungsgerichts [BVerfG] [Federal Constitutional Court] Dec. 12, 2006, 1 BvR 2576/04, NEUE JURISTISCHE WOCHENSCHRIFT [NJW] 878, 2007 (Ger.) (requiring the legislature to amend the law by June 30, 2008).

117. Rechtsanwaltsvergütungsgesetz [RVG] [Attorney Fees Act] § 4a, as amended by Gesetz zur Neuregelung des Erfolgshonorars, July 1, 2008, BGBL. I at 1001, art. 2, § 4a (Ger.).

118. *See* Joachim Teubel, *in* RECHTSANWALTSVERGÜTUNGSGESETZ § 4a, ¶ 24 (Hans-Joachim Mayer & Ludwig Kroiß eds., 4th ed. 2009) (Ger.).

119. *Id.* § 4a, ¶¶ 30–34 (explaining that contingency fees may not be used to let suits go forward that would otherwise not be brought because of the plaintiff's risk aversion and a small probability of success); *see also* Schmolke, *supra* note 16, at 409 (explaining that contingency fees are not permissible in this context).

120. *See* Decreto Legislativo 4 luglio 2006, n. 223, in G.U. 4 luglio 2006, n. 153, as modified by D. Lgs. 4 agosto 2006, n. 248, in G.U. 11 agosto 2006, n. 186 (It.).

121. Codice deontologico forense [Bar Code of Conduct] art. 45 (It.)

nated.[122] However, another section of the civil code still prohibits the assignment of rights and claims contested in litigation to lawyers involved in it.[123] While the law thus allows fees that are (partly) conditional on success, it is not permissible to assign a percentage of the claim to the lawyer.

By itself, however, the contingency fee prohibition does not seem to explain the absence of derivative litigation either. Hertig and McCahery suggest that contingency fees already are "a common but concealed practice throughout Europe."[124] The new Italian law seems to allow at least conditional fees, and derivative suits still have not emerged as a prominent factor.[125] This is illustrated by the emergence of derivative suits in Japan in the early 1990s. Two-part tariffs consisting of a fixed retainer and a fee conditional on success—either in the form of a judgment or a settlement—were seemingly enough to encourage derivative litigation.[126] For Japanese firms representing shareholders, retainers tend to be low and success fees high.[127]

Hence, it appears that the legality of a conditional fee arrangement should suffice to encourage some litigation. The foregoing discussion establishes that some kind of reward is needed for possible plaintiffs to overcome the collective action/free rider problem that is inherent to the corporate structure. Favorable lawyers' fee arrangements, however, are not necessarily the only mechanism that creates incentives either on lawyers or on shareholders to engage in corporate litigation. As I discuss in Part 3, there are other mechanisms of shareholder litigation that have widespread use without derivative litigation, particularly nullification suits in Germany, where the plaintiff's risk is also low compared to the personal benefit. Furthermore, even with high-powered contingency fees in place, there must be a reasonable chance of winning or settling favorably to make the suit worthwhile ex ante for the lawyer. If courts are strongly biased against plaintiffs or plaintiffs have little access to infor-

---

122. C.C. art. 2233(3) (It.) (now only requiring a written agreement between lawyers and clients and no longer prescribing fees based on outcome of litigation).

123. C.C. art. 1261 (It.).

124. Hertig & McCahery, *supra* note 114, at 193.

125. *See* Enriques, *The Comparative Anatomy of Corporate* Law, *supra* note 94, at 1024 (suggesting that the "loser pays" rule has been more important in preventing the emergence of an entrepreneurial plaintiff bar in Europe).

126. *See* West, *Why Shareholders Sue*, *supra* note 15, at 365.

127. *See id.* at 368–72 (noting that, "in practice, many derivative-suit attorneys reduce their retainers").

mation forming the basis for evidence of wrongdoing, suing will still be difficult.

2.2.4. Requirement to Advance Court Fees

The last element of litigation cost that could deter derivative suits is the high up-front fees that a plaintiff has to pay to the court in order to commence the suit. If the amount is high enough, fees of this type will make it difficult to finance a suit. Even a shareholder with a considerable stake might be tempted to reconsider if he is not sure about the action's chance of success. Mark West argued that Japanese derivative litigation was triggered by a 1993 court decision that did away with the previous practice of computing the filing fee as a percentage of the damages sought and replaced it with a relatively modest flat one of only ¥8200.[128] He further suggested that the Japanese courts' practice of frequently requiring plaintiffs to post security for suits allegedly brought in bad faith and led to further deterrence.[129]

A superficial look at the complexities of litigation cost in Europe indicates that the above explanation is plausible in some cases, but does not provide a universal explanation for the scarcity of derivative suits. For example, German courts generally only serve a suit if the fee for the trial is paid.[130] The amount of the fee indeed depends on the amount in dispute, and can generally reach an amount of tens of thousands of Euros if the amount in dispute is several million. For the "lawsuit admission procedure" introduced in 2005, the amount in dispute is usually capped at €500,000, which corresponds to an amount of a few thousand Euros.[131]

---

128. West, *Pricing Shareholder Derivative Actions in Japan & U.S.*, *supra* note 2, at 1463–65; West, *Why Shareholders Sue*, *supra* note 15, at 353. *But see* Dan W. Puchniak & Masafumi Nakahigashi, *Japan's Love for Derivative Actions: Irrational Behavior and Non-Economic Motives as Rational Explanations for Shareholder Litigation*, 45 VAND. J. TRANSNAT'L L. 1, 48–50, 54–56 (2012) (criticizing this explanation because derivative suits apparently began before the change in the fee rules, and suggesting that suits were brought initiated by activist attorneys with non-monetary motivations).

129. West, *Pricing Shareholder Derivative Actions in Japan & U.S.*, *supra* note 2, at 1465–66.

130. GKG § 12(1) (Ger.).

131. The base fee for an amount in dispute of €500,000 is €2,956, with an additional €150 in fees for every additional €50,000. GKG § 34(1) (Ger.) and GKG Anlage 2 (providing a table for the amount of one "value unit" of fees depending on the amount in dispute). In the case of a "normal" lawsuit, this amount is multiplied by 3. GKG Anlage 1, no. 1210 (providing that court fees generally amount to three "value units"), GKG Anlage 1, no. 1640 (establishing a multiplier of 1.0 for an admission procedure under AktG § 148).

In spite of the limit, the amount may be high enough to deter "casual" suits by portfolio shareholders.[132] Furthermore, once the suit has been admitted by the court, fees on the basis of the actual amount in dispute apply, which may result in a substantially larger upfront payment (unless the corporation decides to take over the suit).[133] By contrast, in France, derivative suits are not even hindered by a minimum ownership level, and courts only charge a nominal fee comparable to those in Japan.[134] However, it has been suggested that plaintiffs may be required to advance case-specific cost, e.g., for collecting evidence or for expert witnesses, which may also create a deterrent effect.[135] Nevertheless, as an explanation for the French case, legal fees are much less persuasive. Overall, it is probably safe to say that court fees are a possible deterrent factor, but they are not the only restrictive feature in Germany.[136]

2.3. Access to Information

As discussed in the preceding section, whether the law creates a structure that overcomes the free rider problem inherent in representative litigation depends on how cost rules allocate litigation risk between plaintiffs, firms, and defendants. This other compounding factor is what risk there is, i.e., whether a suit is likely to be successful or not. If meeting the burden of proof is extremely difficult for shareholder plaintiffs, the best incentives set by litigation cost rules may not be enough to encourage suits.

---

132. Peltzer, *supra* note 104, at 955 n.7 (reporting that admission procedures are very rare based on a telephone survey among judges), and *id.* at 957 (arguing that fees will deter shareholders that do not hold a substantial stake).

133. *See* AktG § 148(3) (Ger.); Peltzer, *supra* note 104, at 959–60 (arguing that this possibility further discourages potential plaintiffs). By contrast, in France the courts have found that this is not possible. Cass com. 12-12-2000, 2001 REVUE DES SOCIÉTÉS 323 (Fr.); Germain, *supra* note 24, at 409.

134. *See, e.g.*, *Tarifs des activités judiciaires* [*Rates of Judicial Activities*], GREFFE DU TRIBUNAL DE COMMERCE DE PARIS [REGISTRY OF THE COURT OF COMMERCE OF PARIS] (July 1, 2011), http://www.greffe-tc-paris.fr/judiciaire/tarifs.htm (Fr.) (listing fees for various types of suit in the Paris commercial court). For comparison, the Delaware Chancery Court currently charges a fee of $600 for a derivative suit. *See Court of Chancery Court Fees or Charges*, DEL. STATE COURTS, http://courts.delaware.gov/help/fees/chanceryfees.stm (last visited Apr. 11, 2012).

135. Schmidt, *supra* note 16, at 391.

136. Under some U.S. state laws, plaintiffs can be required to post security for the defendant's expenses. *E.g.*, N.Y. BUS. CORP. L. § 627 (McKinney 2003) (establishing such a requirement for plaintiffs holding less than 5% and shares less than $50,000); *see also* CLARK, *supra* note 7, at 652–55 (discussing how these statutes were introduced to curb abusive litigation).

In some cases, the burden of proof creates particular problems. For example, in Germany, Peltzer has argued that the requirement for plaintiffs to show *dishonesty* or *serious* violations of the law in order to pass the judicial admission procedure and the firm's defense that a suit would not be in the interest of the company create considerable difficulty for plaintiffs.[137] Standards such as the German one or the French requirement to show a "management mistake" are vague and thus create uncertainty while, at least in the German case, leaving a lot of room for the directors to claim spurious reasons why the suit would be harmful.[138] Generally, the main problem seems to be plaintiff's difficulty in obtaining the evidence needed to make a plausible claim, which will typically require the plaintiff to have access to the company's internal documents. Other than in the United States,[139] shareholders normally do not have access to the company's books and records and are limited to the right to ask questions in the shareholder meeting.[140]

More importantly, in the United States, plaintiffs with a thin basis of evidence can avail themselves of pretrial discovery, in the course of which the defendant is required to disclose pertinent information to the plaintiff.[141] Once the suit passes the demand requirement on the basis of relatively limited notice pleading, plaintiffs may rely on information gathered in discovery to coerce the defendant to settle or go to trial.[142] In Europe, a party to a civil suit must generally identify specific documents and ask the court to order the other party to produce them; furthermore, it must explain why these documents are necessary and where they are lo-

---

137. Peltzer, *supra* note 104, at 962–63.

138. Lutter, *supra* note 16, at 765; *see also* Peltzer, *supra* note 104, at 957–58; GUYON, *supra* note 16, at 493 (describing the French "management mistake" standard as vague and unclear).

139. *See, e.g.*, DEL. CODE ANN. tit. 8 § 220 (2011); REVISED MODEL BUS. CORP. ACT [RMBCA] §§ 16.02, 16.03 (1984) (entitling shareholders to inspect and copy corporation's books and records for a proper purpose).

140. Cox & Thomas, *supra* note 34, at 355–56; Paul, *supra* note 104, at 102–03; Giudici, *supra* note 16, at 254.

141. *See* FED. R. CIV. P. 26; Guido A. Ferrarini & Paolo Giudici, *Financial Scandals and the Role of Private Enforcement* 50–51 (Eur. Corp. Gov. Inst., Working Paper No. 40, 2005), *available at* http://ssrn.com/abstract=730403 (explaining that U.S. discovery rules are so far-reaching that they typically shock Continental European lawyers); Frank H. Easterbrook, *Discovery As Abuse*, 69 B.U. L. REV. 635, 636 (1989) (generally discussing the potential abuse in discovery).

142. *See generally* Coffee, *Understanding the Plaintiff's Attorney*, *supra* note 37, at 701–02 (discussing an explanation for the cost differential between plaintiffs and defendants).

cated.[143] The absence of a wide-ranging discovery procedure is often thought to make derivative suits, particularly strike suits, more difficult in Europe.[144] Fishing expeditions are typically not permitted, while "the opponent's obligations to cooperate are usually strict and quite restrictive."[145] A motion to produce a general class of documents will normally not be granted.[146] Mark West reports that in Japan, where U.S.-style discovery also does not exist, shareholders are sometimes able to avoid the information problem by piggybacking on the information brought to light in public enforcement actions.[147]

Is there a Continental European functional equivalent that makes up for this "information gap"? While there is no obvious or complete one, a mechanism that is sometimes brought up by Continental European observers is the appointment of a "special auditor" by a court upon application by minority shareholders.[148] The auditor, who will typically be an accounting professional or other certified expert, is tasked with reviewing problematic or suspicious management activities and subsequently submits a report at the shareholder meeting. The information compiled by the auditor can—at least in theory—form the basis for a lawsuit.

---

143. Nathan M. Crystal & Francesca Giannoni-Crystal, *Understanding Akzo Nobel: A Comparison of the Status of In-House Counsel, the Scope of the Attorney-Client Privilege, and Discovery in the U.S. and Europe*, 11 GLOBAL JURIST 1, 23–24 (2011); *see also* Ferrarini & Giudici, *supra* note 141, at 51–52 (discussing the difference between notice pleading in the United States and fact pleading in Italy, and its implications for shareholder litigation).

144. Enriques, *The Comparative Anatomy of Corporate Law*, *supra* note 94, at 1024; Schmidt, *supra* note 16, at 391 (pointing out that directors control what information the corporation discloses in a French derivative suit); Ferrarini & Giudici, *supra* note 141, at 51, 53; John W. Cioffi, *Adverserialism versus Legalism: Juridification and Litigation in Corporate Governance Reform*, 3 REG. & GOV. 235, 245 (2009).

145. Rolf Stürner, *Transnational Civil Procedure: Discovery and Sanctions against Non-Compliance*, 6 UNIFORM L. REV. 871, 876 (2001).

146. "Only in more exceptional cases, when a party has no exact knowledge of facts and means of evidence in the sphere of its opponent and shows a good cause for an alleged fact . . . the court may order the production and inspection of a category of documents or tangible things." *Id.*

147. West, *Why Shareholders Sue*, *supra* note 15, at 380–81. On a similar process in France, see *infra* Section 3.2.

148. *See* Paul, *supra* note 104, at 103–04 (emphasizing the connection between the purpose of the special audit and the derivative suit).

The corporate laws of all countries discussed here, except Spain, provide for a minority right of this type.[149] The exact procedure and the necessary factual basis vary, but generally there has to be some indication of wrongdoing, and petitioners have to meet a certain minimum ownership threshold. In both France and Germany, the threshold was reduced in recent years, namely from 10% or €1,000,000 to 1% or €100,000 to petition for the appointment of a *Sonderprüfer* in the German 2005 reform,[150] and from 10% to 5% in France in 2001 to initiate an *expertise de gestion*.[151] Belgium also has a 1% (or €1,250,000) threshold,[152] while in Italy (10% and 5% in publicly traded firms),[153] Austria (10%),[154] and Switzerland (10%/CHF 2,000,000) thresholds are relatively high.[155]

(*See table on next page*.)

149. *See* Kalss, *supra* note 30, at 342 ("All legal systems except Spain and England provide for a special audit.") (internal citation omitted). The more far-reaching Dutch inquiry proceedings are discussed in Section 3.3 *infra*.

150. The so-called AktG § 148 I, as amended by UMAG (Ger.); AktG § 142 II (Ger.); *see also* Conac et al., *supra* note 50, at 512 (discussing the threshold reduction). The usual 10% for forcing the corporation into litigation is reduced to 5% if a special audit that brought results to light that indicate liability claims. AKTG § 134(1) (Austria).

Interestingly, there is no such threshold in a German *de facto group*, which allows individual shareholder to ask for an appointment. However, the circumstances when this is possible are fairly limited: either the firm's statutory auditor must have found accounting irregularities, the supervisory board found irregularities with the management's report on group relations, or management board must have declared that disadvantageous transactions were not compensated. *See* AktG § 315 (Ger.).

151. *See* C. COM. art. L. 225-231 (Fr.).

152. CODE DES SOCIÉTÉS art. 168 (Belg.).

153. C.C. art. 2409(1) (It.).

154. *See* AKTG § 130(2) (Austria).

155. OR art. 697(b), para. 1 (Switz.).

Country	Minimum ownership	Note
Austria	10%	
Belgium	1% or €1,250,000	
France	5%	
Germany	1% or €100,000	
Italy	10% 5%	not publicly traded Publicly traded
The Netherlands	10%	more far-reaching "inquiry proceedings" (see section 3.3)
Spain	N/A	
Switzerland	10% or CHF 2,000,000	

Table 2: Minimum ownership thresholds for the appointment of a special auditor

As a true functional equivalent to discovery, special audits seem to fail by and large. The instrument is relatively popular in France, partly because the minority right can be exercised by a shareholder association.[156] Furthermore, under the general law of civil procedure, individual shareholders can also ask the court to appoint an expert even before a trial to establish facts.[157] Elsewhere, special auditors are not appointed frequently, although appointments happen occasionally.[158] Both in Germany and Italy, requirements to show "serious" irregularities put a heavy bur-

156. Holger Fleischer, *Aktienrechtliche Sonderprüfung und Corporate Governance*, 46 RECHT DER INTERNATIONALEN WIRTSCHAFT [RIW] 809, 810–11 (2000) (Ger.) (comparing the frequency of court-appointed audits in France and Germany). Regarding the extensive case law regarding when an appointment is permissible, see MERLE & FAUCHON, *supra* note 22, ¶ 523. In Switzerland, the effectiveness of the instrument is hindered by a statute of limitations, which prohibits derivative suits six months after a shareholder meeting in which the majority approved the "discharge" of the board of directors. OR art. 758, para. 2 (Switz.). This applies even to shareholders who voted against the resolution. This may not leave enough time for an audit to be performed thoroughly. Glanzmann, *supra* note 16, at 175.

157. C.P.C. art. 145 (Fr.); *see* Conac et al., *supra* note 50, at 512 (pointing out that in this case the cost is not borne by the corporation).

158. For Germany, see, for example, Michael Nietsch, *Klageinitiative und besondere Vertretung in der Aktiengesellschaft*, 40 ZGR 589, 592–95 (2011) (Ger.) (discussing the HVB and IKB cases in both of which a special auditor was appointed by a court).

den of proof on the petitioner, which rules out fishing expeditions.[159] In Italy, the court's ability to order the petitioning minority shareholders to provide a deposit to cover cost for the *ispezione giudiziale* may act as a further deterrent.[160] Moreover, since the 2003 reform in Italy, the court can suspend the inspection if the majority replaces the directors and the members of the board of auditors, or *collegio sindacale*, with members who profess to take action to ascertain the alleged violations and eliminate them.[161] Since minority shareholders have no way of forcing the continuation of the outside audit, the majority is in a relatively good position to abort an inspection by replacing the current directors with "friendly" ones who will not allow a suit to proceed.[162]

In general, the minimum threshold seems to be a major hurdle since the percentage required is generally higher than the percentage requirement for a derivative suit.[163] Even France and Switzerland, which allow derivative suits without providing for a minimum threshold, require one for the initiation of a special audit. The higher thresholds for the appointment of the auditor clearly inhibit the effectiveness of this tool for gathering information for a derivative suit.[164]

2.4. Limitations Regarding Potential Defendants

Besides the factors already discussed, it is important to point out that, compared to the United States, derivative actions in Europe are limited in scope, which further reduces their attractiveness for potential plaintiffs who will resort to other instruments. This aspect seems not to have been discussed in the literature yet. In the United States, anyone can be sued derivatively. While the defendant is "usually an officer, director or other

---

159. Schröer, *supra* note 55, § 142, ¶ 10; OBERLANDESGERICHT STUTTGART [OLG Stuttgart] [Stuttgart Higher Regional Court] June 15, 2010, 15 UF 85/10 (Ger.). For Italy, see C.C. art. 2409(1) (It.).

160. C.C. art. 2409(2) (It.).

161. *Id.* art. 2409(3).

162. I thank the participants of the Rome Fordham Alumni Meeting for pointing out this issue to me.

163. *See* Glanzmann, *supra* note 16, at 175–76 (also pointing out that petitioners bear a significant risk of having to pay for the audit); Grechenig & Sekyra, *supra* note 16, at 20 (suspecting that the scarcity of derivative suits in Switzerland may be based on "a percentage limit for initiating an investigation essential for bringing a lawsuit[]").

164. *See* Glanzmann, *supra* note 16, at 175 (suggesting that the shareholders' individual right to launch a derivative suit may be toothless given that they are unlikely to have enough information to form the basis of a suit); Kalss, *supra* note 30, at 342 (arguing that the minimum thresholds for both types of minority rights should be the same).

fiduciary of the corporation," this is by no means a legal prerequisite.[165] The applicable section of the Federal Rules of Civil Procedure—equivalent statutes exist in state law—simply refers to "a right that the corporation or association may properly assert but has failed to enforce,"[166] but says nothing about the defendant or the nature of the suit.[167] Legally, a derivative suit can be any type of suit.

In all of the countries surveyed here, the legal basis for derivative suits is, in all cases, found in a section of the respective corporate law governing directors' liability. This fact has two important consequences. First, derivative suits are only available for claims to damages. The French courts, for example, found that derivative actions are not available for injunctions.[168] The potential of derivative litigation to prevent harmful corporate behavior ex ante and to put pressure on those actually in control of the corporation is therefore low. Of course, this does not imply that shareholders cannot, given the appropriate circumstances, seek judicial recourse to block corporate actions. German courts, for example, recognize, without any specific statutory basis, an individual shareholder's right to enjoin actions taken by the board that infringe in the decision-making power of the shareholder meeting.[169] When the board dutifully sought shareholders' approval, a single shareholder can sue to rescind the decision taken in the shareholder meeting if it is in violation

165. CLARK, *supra* note 7, at 639.

166. FED. R. CIV. P. 23.1(a).

167. Corporate statutes also accept that derivative suits are available against anyone. *E.g.*, DEL. CODE ANN. tit. 8 § 145 (2011), which governs the corporation's power to indemnify for litigation expenses, lawsuits, and settlements. Specifically subsection (b) speaks of suits "in the right of the corporation" and permits that "any person who was or is a party or is threatened to be made a party" can be indemnified under certain circumstances if that person acted as that corporation's fiduciary. *Id.* Thus, the statute implicitly recognizes the derivative suit against anyone. And in fact, experience shows that defendants in many much-publicized important suits (that appear in casebooks) are in fact controlling shareholders (who are alleged to be in violation of their duty of loyalty).

168. *See* Benjamin Mojuyé, *French Corporate Governance in the New Millennium: Who watches the board in corporate France*, 6 COLUM. J. EUR. L. 73, 102, 102 n.94 (2000).

169. Bundesgerichtshof [BGH] [Federal Court of Justice], June 25, 1982, 83 ENTSCHEIDUNGEN DES BUNDESGERICHTSHOFES IN ZIVILSACHEN [BGHZ] 122, 1982 (Ger.); *see* Von Johannes Adolff, *Zur Reichweite des verbandsrechtlichen Abwehranspruch des Aktionärs gegen rechtswidriges Verwaltungshandeln*, 169 ZHR 310 (2005) (Ger.). *Cf.* Katz v. Bregman, 431 A.2d 1274 (Del. Ch. 1981) (granting a shareholder an injunction against the sale of substantially all assets in a direct suit).

of the law.[170] Rescission suits, which will be discussed in Part 3.1, are quite popular across the Continent partly because they allow shareholders to block significant corporate action. In comparison, derivative litigation is not terribly relevant.

Second, possible defendants in Continental European derivative suits are limited to directors (including supervisory board members),[171] and in some cases corporate officers,[172] auditors,[173] or the founders of the corporation.[174] The opportunity to engage with controlling shareholders is therefore limited.[175] True, sometimes controlling shareholders may be sued because they are also directors, and in rare cases a director can be successfully sued for failing to prevent illicit self-dealing by controlling shareholders; the limitation may still, however, prevent litigation that would otherwise be brought.

A possible exception can arise when a controlling shareholder is qualified as a *de facto director* (i.e., a person managing the company and acting like a director without formally having been appointed). This seems to happen occasionally in Italy and France. Consequently, the rules on derivative suits apply.[176] There are, however, considerable limitations. In

170. This includes violations of the controlling shareholders' duty of loyalty and the actionable abuse of majority power where applicable.

171. CODE DES SOCIÉTÉS art. 562 (Belg.); Ley de Sociedades Anónimas art. 134(1) (B.O.E. 1989, 1564) (Spain) (speaking of "liability suits against directors"). In France and Italy, the limitation is implicit since the legal basis for derivative suits (or their equivalents) is in the respective statutory section governing director's liability. C.C. arts. L. 225-249 through 225-257 (Fr.) govern the civil liability of directors and promoters of the corporation. For Italy, see C.C. arts. 2393, 2393bis (It.); ALESSANDRO DE NICOLA, SHAREHOLDER SUITS 177 (2006) (pointing out that only directors, managers, and auditors can be sued derivatively in Italy).

172. Swiss law includes "persons involved in management." OR art. 754, para. 1 (Switz.).

173. *Id.* arts. 754–56; C.C. arts. 2393, 2393bis (It.); Ley de Sociedades Anónimas art. 211 (Spain) (referring to the provisions regarding suits against directors).

174. *See* AktG § 147(1) (Ger.) and AKTG § 134(1) (Austria) (both listing only members of the supervisory and management boards and promoters of the company as potential defendants).

175. *See, e.g.*, Perlman v. Feldmann, 219 F.2d 173 (2d Cir. 1955); *In re* S. Peru Copper Corp. S'holder Derivative Litig., 30 A.3d 60 (Del. Ch. 2011); Kahn v. Kolberg Kravis Roberts & Co., 23 A.3d 831 (Del. 2011); eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1 (Del. Ch. 2010) (derivative suits where the defendant is a shareholder). Derivative suits against shareholders also tend to be easier in private companies. *See, e.g.*, C.C. art. 2476(7) (It.) (providing that shareholders who intentionally approved acts harmful to the corporation are personally liable in an Italian s.r.l.).

176. For Italy, see, for example, FRANCESCO GALGANO & RICCARDO GENGHINI, 1 IL NUOVO DIRITTO SOCIETARIO [THE NEW COMPANY LAW] 483 (2006) (It.); for France, see

Italy, such shareholders can only be sued for actions taken in their capacity as directors, but not for votes cast in the shareholder meeting, etc.[177] In France, courts have permitted suits of this type where the shareholder acted with the intention to harm.[178] Moreover, it may be difficult to qualify a corporate shareholder as a de facto director. In France, where corporations can be appointed as directors,[179] banks have sometimes been qualified as de facto directors even in their role as creditors.[180] However, such a doctrinal move is likely more difficult in the majority of other jurisdictions, where only natural persons can become directors. In any event, proving that a large shareholder qualifies as a de facto director may be hard for an outside investor. Any lawsuit would, therefore, require the plaintiff to overcome another evidentiary hurdle that creates an obstacle for shareholder litigation.

The German law on corporate groups[181] provides a special basis for suits against certain controlling shareholders. Substantively, this law provides that a "controlling undertaking" in a *de facto group* may not instruct a controlled firm to enter into disadvantageous transactions unless the latter is compensated for any disadvantages in the same financial year.[182] In contrast to general corporate law, a minority shareholder can

---

COZIAN ET AL., *supra* note 81, ¶ 262; for Switzerland, see Bundesgericht [BGer] [Federal Supreme Court] Dec. 12, 1991, 117 ENTSCHEIDUNGEN DES SCHWEIZERISCHEN BUNDESGERICTS [BGE] II 570, 571 (Switz.) (finding that the defendants were not de facto directors in this specific case, but implying the possibility of a derivative suit if they were).

177. Conac et al., *supra* note 50, at 510.

178. *Id.*

179. In this case, it has to delegate a specific individual to perform the function on its behalf.

180. MERLE & FAUCHON, *supra* note 22, ¶ 412; COZIAN ET AL., *supra* note 81, ¶ 262; for Switzerland, see Glanzmann, *supra* note 16, at 162–63.

181. The 1965 German *Aktiengesetz* pioneered the idea that corporate groups required special statutory recognition and special mechanisms protecting shareholders and creditors of subsidiaries. AktG §§ 291–328 (Ger.). For a general description, see, for example, Peter Hommelhoff, *Protection of Minority Shareholders, Investors and Creditors in Corporate Groups: The Strengths and Weaknesses of German Corporate Group Law*, 2 EUR. BUS. ORG. L. REV. 61 (2001) (providing an overview of the AktG and its impact on German corporate groups).

182. AktG § 311 (Ger.). The management board of the controlled company is required to prepare a report on relations with other group firms within the first three months of the year, in which all intra-group transactions of the firm are described and compensation received is discussed. This "dependency report" (*Abhängigkeitsbericht*) must be audited by the statutory auditor and the supervisory board, which reports to the shareholder meeting. *See id.* §§ 313, 314. Note that shareholders do not have access to the dependency report.

sue the controlling entity as well as directors of both the controlling firm and the controlled subsidiary on behalf of the corporation.[183] The law neither provides for a percentage limit nor a demand requirement or judicial pre-screening procedure.[184]

There are a number of problems with this model. First, this only applies when the controlling shareholder qualifies as an "undertaking" (*Unternehmen)* that practically controls the dependent firm and where business connections go beyond mere share ownership, thus establishing a *de facto group* that includes both the controlling shareholder and the firm.[185] It is not entirely clear why minority shareholders require stronger protection in this case, as opposed to the situation where a firm is controlled by a private individual or a family.[186] Second, the law has been criticized for actually making it easier for the controlling shareholder to harm the subsidiary, since it explicitly allows disadvantages to the controlled firm as long as there is compensation.[187] Third, it may be difficult to determine what exact advantages and disadvantages resulted from coordinated group policies.[188]

In spite of the procedural advantages, shareholder litigation under the law of corporate groups has remained exceptionally rare. Ulmer, writing in 1999, summarized the state of affairs by saying that the suit had remained "completely without any function in 30 years of its existence."[189] Again, a major reason seems to be the financial risk created by litigation cost.[190] In the absence of a special statute for this type of suit, a plaintiff

---

183. *Id.* §§ 317 III, 318.

184. *Id.* §§ 309 III, IV & 310 IV, 317 IV & 318 IV (all referring to § 309 III to V). The historical reason for the absence of a percentage limit was the impression that it is likely difficult for the required threshold to be met if there is a controlling undertaking. BRUNO KROPFF, AKTIENGESETZ 405 (1965) (Ger.). Holger Altmeppen, *in* 5 MÜNCHENER KOMMENTAR ZUM AKTIENGESETZ § 309, ¶ 121 (Wulf Goette & Mathias Habersack eds., 3d ed. 2010) (Ger.).

185. HÜFFER, *supra* note 22, § 15, ¶ 8.

186. *See, e.g.*, Ulrich Wackerbarth, *Die Abschaffung des Konzernrechts*, 9 DER KONZERN 562–63 (2005) (arguing that the conflict of interests is the same).

187. *Id.* at 564–65.

188. Susanne Kalss, *Alternativen zum deutschen Aktienkonzernrecht*, 171 ZHR 146, 188–89 (2007).

189. Ulmer, *supra* note 19, at 300; *see also* Hirt, *The Enforcement of Directors' Duties*, *supra* note 29, at 191–92 (discussing the experience with shareholder action and its significance in application since its introduction).

190. Altmeppen, *supra* note 184, § 317, ¶ 57. The legislative report on the act also points out that the concern about abusive suits was thought not to be considerable when the law of corporate group was introduced, given that the plaintiff shareholder bears the

shareholder would need to potentially bear court fees computed on the basis of an amount in dispute, which, since the latter amount is usually a damages claim by the corporation, will typically add up to many millions.[191] Even the fee that the plaintiff must pay before the court will serve the suit could, therefore, easily amount to tens of thousands of Euros.[192]

Italy introduced a German-inspired law on corporate groups in 2003.[193] Corporations and other legal entities[194] incur liability by harming subsidiaries whose activities they "direct and coordinate" while acting in their own entrepreneurial interest. Shareholders have a direct but not a derivative claim under Italian law.[195] Again, the burden of proof seems to be a major issue. Ventoruzzo argues that the various elements of the claim are hard to prove, such as the requirement to act in an entrepreneurial interest and to violate the "principles of good management."[196] Furthermore, the rule does not specifically look at the harm done to the firm, but only to the harm to shareholders created by a lower share value (or lost profitability) and losses incurred by creditors if the firm became insolvent.[197]

---

risk of having to reimburse the firm for its cost. KROPFF, *supra* note 184, at 405; Altmeppen, *supra* note 184, § 309, ¶ 121.

191. It is sometimes suggested that AktG § 247(2) (Ger.), which allows the court to reduce the amount in dispute to protect indignant plaintiffs in a nullification suit, should apply by analogy. Altmeppen, *supra* note 184, § 309, ¶¶ 126–28.

192. *See supra* note 131 and accompanying text. Commentators have therefore often argued that the procedures forcing the corporation to bring the suit described above (either under the pre- or the post-2005 law) could be used to enforce claims under the law of corporate groups to lighten the burden resulting from cost risk. *E.g.*, Karsten Schmidt, *Verfolgungspflichten, Verfolgungsrechte und Aktionärsklagen: Ist die Quadratur des Zirkels näher gerückt? Gedanken zur Reform der §§ 147-149 AktG vor dem Hintergrund der Juristentagsdiskussion des Jahres 2000*, 2005 NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT [NZG] [NEW JOURNAL OF CORPORATE LAW] 796, 802 (Ger.); Altmeppen, *supra* note 184, § 317, ¶¶ 63–68 (both arguing that §§ 147 & 148 should apply). However, this theory has never been tested in the courts.

193. C.C. art. 2497 *et seq.* (It.). For an overview, see Paola Fasciani, *Groups of Companies: The Italian Approach*, 4 EUR. COMPANY & FIN. L. REV. 195 (2007).

194. It is not clear whether a natural person can also be sued under this provision. *E.g.*, Fasciani, *supra* note 193, at 223 (discussing the controversy). Ventorozzo points out that many Italian firms are controlled by individuals, which renders the rule somewhat irrelevant. Ventoruzzo, *supra* note 68, at 251.

195. *See* Guido Ferrarini, Paolo Guidici & Mario Stella Richter, *Company Law Reform in Italy? Real Progress,* 69 RABELSZ 659, 694 (2005) (Ger.).

196. Ventoruzzo, *supra* note 68, at 252.

197. Ferrarini et al., *supra* note 195, at 695.

3. THE PATH OF LEAST RESISTANCE: DO WE NEED DERIVATIVE LITIGATION?

The previous section illustrates that there are at least four different obstacles to shareholder derivative litigation in Continental Europe. Addressing a single one of them would likely not suffice to encourage this type of litigation. Hence, based on the sparse use of derivative suits in Continental Europe, one may conclude that corporate law is inadequately enforced in Continental Europe. From the American perspective, the scarcity is startling, since in the United States the derivative suit is a major enforcement mechanism for corporate law. In this Section, I suggest that this situation is not quite as bad as one might believe. Other mechanisms at least partly make up for this shortfall in enforcement and possibly create at least some deterrence against wrongdoing by managers and controlling shareholders. However, it would be premature to conclude that there are effective functional equivalents in all cases. Without attempting to provide a complete picture, the following subsections explore three enforcement mechanisms. Part 3.1 discusses the nullification suit, which is common across the European continent and has been discussed with particular intensity in Germany, given that it is often claimed that many of these suits are abusive. Part 3.2 looks at the role of criminal investigations using the example of France, where criminal investigations play a particularly important role. Part 3.3 discusses the Dutch "inquiry proceedings," an instrument standing between public and private enforcement, where shareholders can induce a court to investigate managerial wrongdoing.

3.1. Rescission Suits

The private instruments of choice in much of Continental Europe are suits permitting shareholders to rescind or nullify decisions made in the shareholder meeting, and sometimes those of the board, because these decisions violate the law—including the majority shareholder's duty of loyalty—or the company's articles.[198]

The rescission, or nullification, suit is of considerable significance in several Continental European countries given the frequency of share-

---

198. For the legal basis of these lawsuits see AktG §§ 241–57 (Ger.); C. COM. art. L. 235-1 (Fr.); C.c. arts. 2377–79 (It.); OR arts. 706, 708 (Switz.); Ley de Sociedades Anónimas art. 115 (B.O.E. 1989, 1564) (Spain); CODE DES SOCIÉTÉS art. 178 (Belg.); BURGERLIJK WETBOEK [BW] [CIVIL CODE] arts. 2:13–2:16 (Neth.); AKTG §§ 195–202 (Austria). Laws often explicitly distinguish between resolutions that are void and those that can be avoided.

holder votes. Shareholders generally need to vote on more issues than their American counterparts. Like in the United States, European shareholders vote on election and removal of directors,[199] mergers,[200] and changes to the articles.[201] Changes to the articles include increasing the company's capital, which is necessary to issue new shares,[202] and reductions of capital.[203] Furthermore, shareholders vote on the waiver of preemptive rights[204] and the election of the company's auditor.[205] In France, Belgium, Italy, Switzerland, the Netherlands, and Spain, shareholders also vote on the approval of financial statements,[206] and in Germany and Austria, shareholders do so in the case of a disagreement between the

---

199. AktG § 103 (Ger.); C. COM. art. L. 225-18 (Fr.); AKTG § 87 (Austria); Ley de Sociedades Anónimas arts. 123, 131 (Spain); C.C. art. 2364(2) (It.); CODE DES SOCIÉTÉS art. 518(2), (3) (Belg.); BW arts. 2:132, 2:134 (Neth.).

200. Umwandlungsgesetz [UmwG] [Reorganization Act], Oct. 28, 1994, BGBL. I at 3210, §§ 13, 65 (Ger.) (requiring a supermajority of three quarters); C. COM. art. L. 236-2 (Fr.); AKTG § 221 (Austria); FUSIONSGESETZ [FUSG] [MERGER ACT] Oct. 3, 2003, arts. 18(a), 43, 64(a) (Switz.) (requiring a two thirds supermajority); Ley 3/2009 de 3 de abril sobre modificaciones estructurales de las sociedades mercantiles arts. 8, 40 (B.O.E. 2009, 3) (Spain); C.C. art. 2365 (It.); CODE DES SOCIÉTÉS art. 699 (Belg.); BW art. 2:317 (Neth.).

201. *See* AktG § 179 (Ger.); C. COM. art. L. 225-96 (Fr.); AKTG § 145 (Austria); OR art. 647 (Switz.); Ley de Sociedades Anónimas art. 144 (Spain); C.C. art. 2365 (It.); CODE DES SOCIÉTÉS art. 558 (Belg.); BW art. 2:121 (Neth.).

202. *See* AktG §§ 182, 192, 202 (Ger.); C. COM. arts. L. 225-129, L. 225-130 (Fr.); AKTG §§ 149, 159, 169 (Austria); OR art. 650, 651, 653, para. 1 (Switz.); Ley de Sociedades Anónimas art. 152.1 (Spain); CODE DES SOCIÉTÉS art. 581 (Belg.); BW art. 2:96 (Neth.); Council Directive 77/91, art. 25, 1976 O.J. (L 26) 1, 8 (EC).

203. *See* AktG §§ 222, 229, 237 (Ger.); C. COM. art. L. 225-204 (Fr.); AKTG § 175 (Austria); OR art. 732 (Switz.); Ley de Sociedades Anónimas art. 164.1 (Spain); CODE DES SOCIÉTÉS art. 612 (Belg.); BW art. 2:99 (Neth.).

204. *See* AktG § 186(3) (Ger.); C. COM. art. L. 225-135 (Fr.); AKTG § 153(3) (Austria); OR art. 652b (Switz.) (permitting the shareholder meeting to waive the preemptive right for an important reason); Ley de Sociedades Anónimas art. 159.1 (Spain); C.C. art. 2441 (It.); CODE DES SOCIÉTÉS art. 596 (Belg.); BW art. 2:96a(6) (Neth.).

205. HANDELSGESETZBUCH [HGB] [COMMERCIAL CODE], Oct. 15, 1897, REICHSGESETZBLATT [RGBL] 219, as amended Dec. 22, 2011, BGBL. I 3044, § 318 (Ger.); C. COM. arts. L. 225-228, L 823-1 (Fr.); UNTERNEHMENSGESETZBUCH [UGB] [BUSINESS ENTERPRISE CODE], Oct. 15, 1897, RGBL. 219 (Ger.) (as HGB), introduced in Austria, Dec. 24, 1938, RGBL. I 1428, renamed UGB, Oct. 27, 2005, BGBL. I No. 120/2005, as amended BGBL. I No. 35/2012 , § 270 (Austria); OR art. 730 (Switz.); Ley de Sociedades Anónimas art. 204 (Spain); BW art. 2:393(Neth.). The vote is a requirement of EU law. EU Audit Directive 2006/43/EC of May 17, 2006, O.J. l 157/87, art. 37.

206. C. COM. art. L. 225-100 (Fr.); OR art. 698(3) (Switz.); Ley de Sociedades Anónimas art. 212 (Spain); C.C. art. 2364(1) (It.); CODE DES SOCIÉTÉS art. 554 (Belg.); BW arts. 2:117(5), 2:362(6) (Neth.).

supervisory and the management board.[207] It is also typically required that shareholders vote on the distribution of dividends.[208] Finally, in European companies, shareholders often vote on annual "discharge" resolutions regarding directors, which do not extinguish liability in most jurisdictions, but imply general approval of the board.[209] These votes are often, but not in all countries, explicitly required by the law.[210]

Of course, suits to determine the validity of a shareholder resolution are possible in the United States as well.[211] But given the larger number of significant shareholder votes and the prevalence of concentrated ownership structures in Continental Europe, these suits address some of the issues that would be litigated in shareholder derivative suits or class actions take in the United States, thus making the absence of such suits a much less significant concern. Under concentrated ownership, shareholder resolutions are typically passed with the vote of majority shareholders or a coalition of large shareholders, who are effectively able to put the board in place and to determine corporate policies. While the formal defendant in a suit of this type is the corporation,[212] they are de facto directed against the corporation's majority shareholders.[213] For example, in France, the doctrine of *abus de majorité,* which limits the power of majority shareholders to act in their own interest, developed largely as a result of rescission suits.[214] In Germany and Italy, these lawsuits have become so widespread that legislative measures have been

207. *See* AktG § 173 (Ger.); AKTG § 104(3) (Austria); for France see, for example, MERLE & FAUCHON, *supra* note 22, ¶ 481 (discussing "quitus"). If an Italian company uses the German-inspired dualistic system, shareholders do not vote on the financial statements.

208. *See* AktG § 58 (Ger.); C. COM. art. L. 232-11 (Fr.); AKTG § 104(2)(2) (Austria); OR art. 698, para. 4 (Switz.); Ley de Sociedades Anónimas art. 213 (Spain); C.C. art. 2364bis(1)(4) (It.).

209. Among the countries surveyed here, Belgium seems to be the only one where a discharge resolution extinguishes liability. *See* Bertrand & Coibion, *supra* note 44, at 283–84, 287.

210. AktG § 120(1) (Ger.); AKTG § 104(2)(3) (Austria); OR art. 698, para. 5 (Switz.); CODE DES SOCIÉTÉS art. 554 (Belg.); EUGENIA UNANYANTS-JACKSON, DIRECTORS' LIABILITY DISCHARGE PROPOSALS: THE IMPLICATIONS FOR SHAREHOLDERS 28, 31 (Sarah Wilson ed., 2008) (pointing out that discharge resolutions are common also in the Netherlands and Spain, but do not extinguish directors' liability).

211. *See, e.g.*, DEL. CODE ANN. tit. 8 § 225 (2011).

212. *See* van Aaken, *supra* note 31, at 302; Luca Enriques, *Do Corporate Law Judges Matter? Some Evidence from Milan*, 3 EUR. BUS. ORG. L. REV. 765, 784 (2002) [hereinafter Enriques, *Do Corporate Law Judges Matter?*].

213. Enriques, *Do Corporate Law Judges Matter?*, *supra* note 212, at 784.

214. Germain, *supra* note 24, at 412; GUYON, *supra* note 16, at 488.

taken to curb alleged abuse.[215] Generally, nullification suits do not require the plaintiff shareholder to hold a certain percentage of shares.[216] Only in 2003 did Italy introduce a threshold of 5% for unlisted and 0.1% for listed companies.[217] Rescission suits are sometimes limited by a short prescription period, e.g., one month after the meeting in Germany for most suits,[218] ninety days in Italy,[219] but three years in France.[220]

In Germany, allegedly abusive litigation by so-called "predatory shareholders"[221] continues to cause debate and resulted in the production of voluminous literature. In 2010 alone, 70 publicly-traded companies were sued.[222] For the years 2006 through 2008, Vermeulen and Zetzsche report 135, 164, and 163 suits respectively, which is by all means not a negligible number given that 752 German companies were listed in regu-

---

215. Abuse has also been an issue elsewhere. *See* Klaus J. Hopt, *Shareholder Rights and Remedies: A View from Germany and the Continent*, 1 COMPANY FIN. & INSOLVENCY L. REV. 261, 268 (1997) (reporting that abuse has become common in France and Belgium as well, although the issue was dealt with by the courts and has received less attention from academic commentators); GUYON, *supra* note 16, at 490–91 (discussing the abuse of legal rights of minority shareholders in France); *see also* Bertrand & Coibion, *supra* note 44, at 498 (reporting a "significant amount" of suits in Belgium).

216. AktG § 245(1) (Ger.); AKTG § 196(1)(1) (Austria) (both providing that a shareholder who submitted a written objection in the shareholder meeting has standing); OR art. 406 para. 1 (Switz.); CODE DES SOCIÉTÉS art. 178 (Belg.); BW art. 2:15(3)(a) (Neth.) (both providing that a person with a legal interest can sue); Ley de Sociedades Anónimas (B.O.E. 1989, 1564) art. 117 (Spain); *see* Germain, *supra* note 24, at 412; CHAVARÉT ET AL., *supra* note 79, ¶ 28353 (both explaining that in France, the party the law intends to protect can sue).

217. C.C. art. 2377(3) (It.). Since 1975, a 5% threshold has prevented—and still prevents today—small shareholders of listed companies from challenging the validity of resolutions approving annual accounts of listed companies on the grounds that the companies fail to conform with the provisions governing the preparation thereof, provided that the company's auditor has judged the accounts to be consistent with such provisions and generally accepted accounting principles. *See* Enriques, *Do Corporate Law Judges Matter?*, *supra* note 212, at 785–86.

218. AktG 246(1) (Ger.).

219. C.C. art. 2377(6) (It.). There are longer limitation periods for violations of the law that are so fundamental that they are not considered just voidable, but void. *See* AktG 242(2) (Ger.) (three years). For Italy, see GALGANO & GENGHINI, *supra* note 176, at 393 (three years).

220. C. COM. art. L. 235-9 (Fr.).

221. The German term is "räuberischer Aktionär." *See, e.g.*, Burkhard Hess & Christoph Leser, *"Räuberische" Aktionäre—Ist das Prozessrecht hilflos?*, *in* FESTSCHRIFT FÜR UWE H. SCHNEIDER, *supra* note 16, at 519.

222. Walter Bayer & Thomas Hoffmann, *Beschlussmängelklagen: Rechtstatsachen aus 2010*, 2011 DIE AKTIENGESELLSCHAFT (AG-REPORT) R175, R175.

lated markets and 450 were traded in open markets in 2008.[223] Most of these suits are brought by a small circle of about 40 repeat plaintiffs.[224] Baums et al. report 580 suits in publicly traded firms between July 1, 2007 and July 30, 2011.[225]

Rescission suits are attractive because their disruptive potential creates an effective bargaining tool for the plaintiff against the firm and dominant shareholders.[226] While the suit is pending, plaintiffs can enjoin the transaction that has been voted on, thus often preventing the transaction from proceeding.[227] Even a pending lawsuit relating to the firm's annual decisions—such as the discharge resolution—the election of the auditor, or the payment of dividends, can be bothersome.[228] It is thus often alleged that certain plaintiff shareholders bring lawsuits basically to "to blackmail companies into lucrative settlement agreements."[229] Most academic commentators seem to believe that the majority of rescission suits in Germany are abusive.[230] Instead of suing derivatively, "predatory shareholders" are alleged to excessively use shareholder rights in the formal meeting to provoke formal mistakes that are grounds for rescission suits.[231] Some firms are reported to have preemptively paid "professional plaintiffs" to not attend the annual general meeting.[232]

---

223. Erik P.M. Vermeulen & Dirk A. Zetzsche, *The Use and Abuse of Investor Suits*, 7 EUR. COMPANY & FIN. L. REV. 1, 24–25 (2010).

224. Theodor Baums, Astrid Keinath & Daniel Gajek, *Fortschritte bei Klagen gegen Hauptversammlungsbeschlüsse*, 28 ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT [ZIP] [JOURNAL OF BUSINESS LAW] 1629, 1635–37 (2007) (Ger.) [hereinafter Baums et al., *Fortschritte bei Klagen*] (listing the names of repeat plaintiffs).

225. Theodor Baums, Florian Drinhausen & Astrid Keinath, *Anfechtungsklagen und Freigabeverfahren. Eine empirische Studie,* 32 ZIP 2329, 2331 (2011) (Ger.) [hereinafter Baums et al., *Anfechtungsklagen und Freigabeverfahren*].

226. Conac et al., *supra* note 50, at 513.

227. *Id.* at 513; *see* C.C. art. 2378(3) (It.) (plaintiffs may petition court to order directors not to execute the resolution). For Germany, see HÜFFER, *supra* note 22, § 243, ¶ 66. The trial court may issue an injunction halting the registration in the register of companies under ZPO §§ 935–45 (Ger.).

228. Baums et al., *Anfechtungsklagen und Freigabeverfahren*, *supra* note 225, at 2337 (noting an increase in the number of suits attacking the election of the auditor).

229. Conac et al., *supra* note 50, at 513.

230. *E.g.*, Hopt, *supra* note 215, at 267 ("Since the late 70s this has become a plague."); Vermeulen & Zetzsche, *supra* note 223, at 60 (finding that most suits between 2005 and 2008 qualified as abusive, using criteria such as the person of the plaintiff, the type of legal counsel, the nature of the complaint, and backing by institutional shareholders).

231. Hess & Leser, *supra* note 221, at 522.

232. *Id.* at 521–22.

A rescission lawsuit can be particularly disruptive when a corporation needs shareholder approval to issue new shares or to reduce the firm's capital since these measures cannot be recorded in the company register while the suit is pending.[233] Germany, therefore, introduced a "clearance procedure" (*Freigabeverfahren*) in 2005, thus allowing the court to let an increase or reduction of capital, or the integration of a corporation into a contractual group to go ahead in spite of a pending suit. The court may grant the corporation's motion "if the suit is patently baseless, or if the alleged violations of the law are less onerous to the firm and its shareholders than the disadvantage of the transaction grounding to a halt."[234] The introduction of a percentage threshold in Italy was motivated by similar concerns.

Given the scarcity of derivative suits in Germany, even after the 2005 reform, the omnipresence of rescission suits provides a puzzle, but only at first glance. There are four distinct advantages. First, as already explained, a shareholder can relatively easily "harass" the corporation with suits of this type. Second, the absence of a minimum ownership threshold may play a role in comparison to derivative suits (but not in comparison to suits under the law of corporate groups). Third, the substantive case for a claim is easier to make. A plaintiff does not need to show a "serious" violation of a law to pass a judicial prescreening procedure as he would to bring a derivative suits. Many suits rest on claims that the corporation failed to follow the appropriate procedure (e.g., by providing

---

233. *E.g.*, Thorsten Helm & Nikolaus Vincent Manthey, *Missbräuchliche Anfechtungsklagen im Aktienrecht—Rechtsvergleich und Lösungsansätze*, 2010 NZG 415, 415 (Ger.).

234. Conac et al., *supra* note 50, at 514; § 246a AktG, as amended by UMAG, Sept. 22, 2005, BGBL. I at 2802 (Ger.); *see also* Till Naruisch & Fabian Liepe, *Latest Developments in the German Law on Public Companies by the Act on Corporate Integrity and Modernisation of the Right of Resolution-Annulment (UMAG)—Shareholder Activism and Directors' Liability Reloaded*, 2007 J. BUS. L. 225, 231–32 (discussing the express release procedure under Aktiengesetz). The procedure was reformed with the Gesetz zur Umsetzung der Aktionärsrechterichtlinie (ARUG), July 30, 2009, BGBL. I at 2479 (Ger.). The new law, among other things, requires the petitioner to show that he owned shares corresponding to a legal capital of €1,000 since the time when the meeting was called. *See* Baums et al., *Anfechtungsklagen und Freigabeverfahren*, *supra* note 225, at 2348–49 (providing empirical data the prevalence and effectiveness of the procedure).

Similarly, the Italian corporate law reform of 2003 specified that the judge has to decide upon a petition to block a shareholder resolution by comparing the prejudice the plaintiff would suffer following execution with the prejudice the company would suffer from not executing the resolution. *See* C.C. art. 2497 *et seq.* (It.); *see also* Fasciani, *supra* note 193, at 211–12.

inadequate disclosure to shareholders before the general meeting).[235] However, alleged violations of substantive standards such as the duty of loyalty also play a role.[236]

Fourth, the cost risk is limited and foreseeable. In principle, the English Rule applies to these lawsuits as well, the defendant being the corporation.[237] However, the amount in dispute—which determines the amount of court fees the plaintiff has to advance—is limited to the lower of 10% of the corporation's nominal capital or €500,000.[238] The limitation is therefore similar to the one in the preliminary procedure to admit a derivative suit (see above Section 2.2), but unlike in the latter case, there is no second stage of litigation where the amount in dispute could reach many millions, and the cost therefore is limited to tens of thousands of Euros. Theodor Baums argues that the risk of having to bear cost will therefore deter "occasional," but not "professional," plaintiffs.[239] For the latter group, the possibility to put pressure on the corporation creates an equivalent incentive for plaintiffs to take action, as the contingency fee does for derivative suits in the United States.

3.2. Criminal Investigations

Another important alternative is shareholders' ability to "piggyback" on criminal investigations. In France, directors' duties are often thought to be subject to stronger scrutiny under criminal law than equivalent duties in other countries.[240] This does not imply that the risk of criminal liability in general is the greatest in France. This honor may in fact go to the United States, where violations of disclosure duties under the securities law carry strong criminal sanctions.[241] By contrast, the French crime of *abus de biens sociaux* (abuse of corporate assets) penalizes directors' misuse of the company's property and credit in bad faith, "when direc-

---

235. *See* Baums et al., *Fortschritte bei Klagen*, *supra* note 224, at 1640–41 (providing data about professed reasons for the suits).

236. *Id.*

237. Theodor Baums, *Die Prozesskosten der aktienrechtlichen Anfechtungsklage*, *in* FESTSCHRIFT FÜR MARCUS LUTTER zum 70. GEBURTSTAG 283, 284 (Uwe H. Schneider, Peter Hommelhoff, Karsten Schmidt, Wolfram Timm, Barbara Grunewald & Tim Drygala eds., 2000) (Ger.) [hereinafter Baums, *Die Prozesskosten*].

238. § 247 I AktG (Ger.).

239. Baums, *Die Prozesskosten*, *supra* note 237, at 296.

240. *See, e.g.*, James A. Fanto, *The Role of Corporate Law in French Corporate Governance*, 31 CORNELL INT'L L.J. 31, 85 (1998) (quoting Senator Marini's observation that "French corporate law is extremely criminalized").

241. Securities Exchange Act of 1934 § 32(a), *as amended in* 15 U.S.C. § 78ff(a) (2006).

tors knew that it was contrary to its interest."[242] Hence, prosecutors and courts look at the substance of managerial decision-making.

Criminal sanctions used to enforce directors' duties are not unique to France. Italian *infedeltà patrimoniale*[243] and German *Untreue*,[244] both meaning "disloyalty," serve a similar function at least in part.[245] French law, however, has been most widely discussed, particularly with respect to how minority shareholders can initiate criminal prosecution by filing a criminal complaint (*plainte avec constitution de partie civile*). Shareholders can attach themselves to the prosecution in order to receive compensation for damages.[246] As explained by Conac et al., "[i]n order for the complaint to be admissible, it is enough that the circumstances which gave rise to the complaint allow the examining magistrate to consider 'possible' the existence of the damage to the company and the link with the alleged abuse of corporate assets."[247] If this criterion is met, the examining magistrate has the duty to investigate.[248] The examining judge also has the right to access the company's documents, which solves the information problem shareholders otherwise would have to overcome. There were between 416 and 480 convictions per year between 2000 and 2006, of which an estimated 20% have led to actual jail time.[249] While it is likely that these are mostly small firms, it is potentially relevant for large firms as well. Recent developments have also made it easier for Italian shareholders to similarly file a criminal complaint by way of the so-called "*parte civile*."[250]

In recent years, dissatisfaction with the extent of criminal liability risk has grown in France, which is why the government commissioned a re-

---

242. C. COM. L. 242-6 (Fr.). The maximum penalty is five years in prison. For a doctrinal description in English see Nicole Stolowy, *Company-Related Offences in French Legislation*, 2007 J. BUS. L. 1, 3–7.

243. *See* C.C. art. 2634 (It.).

244. STRAFGESETZBUCH [STGB] [PENAL CODE], Aug. 21, 1995, BGBL. I, as amended, § 266 (Ger.).

245. *See, e.g.*, Conac et al., *supra* note 50, at 520–22 (discussing German and Italian law).

246. GUYON, *supra* note 16, at 497 (explaining that shareholders often prefer to obtain damages this way); DE NICOLA, *supra* note 171, at 146; Bernard Black et al., *Legal Liability of Directors Part 2*, 2008 COLUM. BUS. L. REV. 1, 18–19.

247. Conac et al., *supra* note 50, at 518.

248. *Id.* at 518.

249. *Id.* at 519.

250. *Id.* at 522 (referring to Cass., sez. V, 16 giugno 2006, n. 37033, Giur. comm. 2007, 1030 (It.) where shareholders are qualified as victims and therefore enabled to file a petition to the court).

port on the "decriminalization" of business law published in 2008. The core corporate infraction of *abus de biens sociaux,* however, was to remain in place according to the report.[251] At least for now, the decriminalization project has been shelved. Overall, criminal redress often seems to assume the function of enforcing the duties of directors and officers, both in terms of deterrence and permitting the recovery of damages. It appears to be superior for shareholders, given that it involves no court fees or litigation risk, and that it also helps to overcome the information problem solved by discovery in the United States.

3.3. The Dutch Inquiry Proceedings

Dutch law provides another interesting model that combines a privately instigated judicial investigation with enforcement and is widely thought to be successful. While there is no derivative suit under Dutch corporate law,[252] minority shareholders can petition the enterprise chamber (*ondernemingskamer*), a special division of the Amsterdam Court of Appeals, to launch an official investigation. A petition for an investigation can be brought, among other situations, to conduct an investigation into the business policies and the conduct of affairs of a legal person, i.e., when there is a problem with the company's management (*enquête* or inquiry proceedings).[253] A similar procedure can be launched to challenge the accuracy of a corporation's financial statements.[254]

A petition to start inquiry proceedings can be brought either by the advocate general of the court for reasons of public policy,[255] by a labor union,[256] or by shareholders holding the lower of a nominal capital of €225,000 or a 10% share in the company.[257] The petitioner has to submit a written request stating why he believes that the company was being mismanaged. At that point, control and initiative over the investigation pass to the court.[258] If the enterprise chamber finds that the petition is

---

251. JEAN-MARIE COULON ET AL., LA DÉPÉNALISATION DE LA VIE DES AFFAIRES 31–37 (2008) (Fr.).

252. SCHUIT ET AL., *supra* note 43, at 155.

253. BW art. 2:345(1) (Neth.).

254. *Id.* art. 2:447 (Neth.). Furthermore, similar procedures can be used as redress in situations of conflict relating to the removal of directors (*Id.* arts. 2:158, 2:161a (Neth.)), and to review the fairness of freezeouts. *Id.* art. 2:92a (Neth.).

255. *Id.* art. 2:345(2) (Neth.).

256. *Id.* art. 2:347 (Neth.).

257. *Id.* art. 2:346(b) (Neth.).

258. SCHUIT ET AL., *supra* note 43, at 157.

sufficiently substantiated, it appoints investigators.[259] On the basis of the investigators' report, the enterprise chamber determines whether the case amounts to "misconduct" and requires further action.[260] The enterprise chamber can take an array of measures, including the dismissal of board members, the rescission of board or shareholder resolutions, the appointment of temporary board members, and even the dissolution of the company.[261] While damages cannot be awarded in these proceedings, the corporation may subsequently ask the court to have the director responsible for "a wrong policy or an unsatisfactory state of affairs" to indemnify the corporation for the costs of the proceedings.[262] Furthermore, successful inquiry proceedings may tarnish a director's reputation and will consequently facilitate liability suits.[263]

Interestingly, the *inquiry proceeding* has become reasonably common in spite of the high 10% threshold: in publicly traded firms alone, there were twenty-three cases from 2000 to 2007,[264] nineteen of which were brought by minority shareholders, such as institutional investors and the Dutch Investors' Association.[265] Commentators argue that the main driver was that injunctive relieve became available in 1994 and has since become the rule, and often the de facto final decision, in disputes between majority and minority shareholders.[266] Since then, the enterprise chamber acquired a reputation for resolving conflicts in a speedy manner

---

259. Vermeulen & Zetzsche, *supra* note 223, at 16.

260. BW art. 2:356 (Neth.). Some jurisprudence revolves around the question what constitutes misconduct. While the enterprise chamber recognizes the need for managerial discretion with respect to company policies, the violation of minority shareholders' rights generally qualifies. L. Timmerman & A. Doorman, *Rights of Minority Shareholders in the Netherlands*, 6 ELECTRONIC J. COMP. L. 181, 199–202, nn.24–25 (Dec. 2002), *available at* http://www.ejcl.org/64/art64-12.html.

261. BW art. 2:356 (Neth.); Martijn van Empel, *The Netherlands*, *in* THE LEGAL BASIS OF CORPORATE GOVERNANCE IN PUBLICLY HELD CORPORATIONS 123, 147 (Arthur Pinto & Gustavo Visentini eds., 1998); SCHUIT ET AL., *supra* note 43, at 159.

262. BW art. 2:354 (Neth.).

263. *See* Maarten J. Kroeze, *The Companies and Business Court as a Specialized Court*, *in* THE QUALITY OF CORPORATE LAW AND THE ROLE OF CORPORATE LAW JUDGES 143, 147 (Louis Bouchez, Marco Knubben, Joseph McCahery & Vino Timmerman eds., 2006).

264. Vermeulen & Zetzsche, *supra* note 223, at 17. Before 2000, inquiry proceedings were much rarer. *Id.*

265. *Id.* at 58.

266. *See* Kroeze, *supra* note 263, at 149; Vermeulen & Zetzsche, *supra* note 223, at 18–20; Joseph A. McCahery & Erik P.M. Vermeulen, *Conflict Resolution and the Role of Corporate Law Courts: An Empirical Study*, *in* COMPANY LAW AND SMES 207, 239–40 (Mette Neville & Karsten Engsig Sørensen eds., 2010); *see also* BW art. 2:349a (Neth.).

and coming to reasonable and pragmatic solutions.[267] Cost is not a deterrent factor, since expenses are by default borne by the firm; however, the court may order the petitioner to indemnify the firm if the petition was not made on well-founded grounds.[268] Moreover, the comparatively high threshold of 10% most likely also prevents abusive petitions, given that such a high ownership stake typically indicates a strong commitment to the firm. Nevertheless, the inquiry proceeding has become an important mechanism for corporate law enforcement in the Netherlands that is widely considered a success, thus making the absence of a derivative suit mechanism a less pressing problem.

CONCLUSION

In my contribution to the symposium, I have attempted to demonstrate two things. First, the absence of derivative suits in Continental Europe cannot be explained with a single factor, but only with a whole range of elements that make them unavailable or render derivative suits unattractive to small shareholders. A version of the "Anna Karenina principle" applies analogously; in other words, several prongs have to be met to make a particular type of suit attractive. This is the case in the United States, but not in Continental Europe. Second, the dearth of derivative suits does not necessarily mean that there is no corporate law enforcement, but rather that shareholders are likely to choose the "path of least resistance" (section 3) and use other methods to address grievances.

Specifically, I have identified four necessary factors, which are as follows: the presence of liberal standing requirements, as opposed to European minimum ownership thresholds; a litigation cost structure that sets incentives that overcome the collective action problem; availability of information to plaintiffs; and the ability to sue those who actually control the firm, which in Europe often includes large shareholders.

The most complicated factor, the allocation of litigation cost and risk, has three aspects. A considerable upfront cost can deter many suits. Between the other two factors, the "English Rule" of litigation cost and the availability of contingency fees, there are strong reasons to believe that contingency fees are more important given that the distinctions between the American and the English Rule are smaller than one might think at first glance. By contrast, contingency fees illustrate the importance of setting strong incentives for a private actor (such as a lawyer or a repeat

---

267. *See* Kroeze, *supra* note 263, at 149; McCahery & Vermeulen, *supra* note 266, at 241–43.

268. BW art. 2:354 (Neth.).

plaintiff). Other examples include conditional fees in Japanese shareholder litigation and rescission suits brought by shareholders in Germany. In the latter example, the motivation is also not the shareholder's proportionate benefit from the shareholder's stake of the firm, but personal advantages that the plaintiff can obtain in a settlement. As in the United States, there is an extensive debate regarding abusive suits by repeat plaintiffs and their illegitimate motives. Viewing both systems positively, one can suspect that plaintiffs need to be incentivized with a reward that exceeds their individual share in the social harm. In a system of private enforcement, plaintiffs are bounty hunters that need to be promised a reward. The problem is that bounty hunters sometimes set excessive enforcement actions and cause collateral damage.

This Article shows that there are other systems of enforcement of corporate law in Continental Europe. Some of these, such as rescission suits, are primarily private, and some are public, such as criminal enforcement. The prevalence of private mechanisms demonstrates that we do not need a "cultural" theory of corporate law to explain why derivative suits have not spread as widely in Europe as they have in the United States. The case of the rescission suit, most of all in Germany, does not support the hypothesis that Europeans are inherently less litigious than Americans, but rather indicates that the right incentives set by the institutional framework are decisive. The eclectic presentation of partly functional equivalent mechanisms of course does not demonstrate that Continental European corporate law is equally well enforced. For example, rescission suits may capture issues that are important enough to warrant a shareholder vote, but not violations of directors' fiduciary duties that happen below the radar screen of the shareholder meeting. Furthermore, the absence of derivative suits seems to imply that Continental European private enforcement mechanisms suffer from the inability of plaintiffs to obtain sufficient information. While private enforcement mechanisms often invite excessive use, public mechanisms may tend to under-enforce and weaken incentives to vigorously pursue wrongdoing by directors, managers, and controlling shareholders. No system is perfect, and a global assessment is beyond the scope of this contribution.