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The conflicting approaches of Bulgarian courts to the right of shareholders to convoke a general meeting in non-listed joint-stock companies

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A. Introduction

Non-listed joint stock companies are an important type of corporate entity for medium and large-scale investors in Bulgaria. While shareholder rights in listed joint-stock companies are subject to detailed legal harmonization in the European Union, including under Directive 2007/36/EC on the exercise of certain rights of shareholders in listed companies, potential hindrances towards the exercise of shareholder rights in non-listed joint stock companies might be harder to identify for investors, especially foreign ones. As a result, regard must be had for any divergent case law regarding the exercise of shareholder rights.

This paper analyses a series of cases demonstrating two conflicting approaches of Bulgarian courts towards the effective and practical exercise of the right of shareholders to convoke a general meeting in a non-listed joint stock company. First, a general overview of this right will be provided. Second, through analysis of case law, certain conflicting points in the exercise of this right will be identified. Finally, the paper will present the conclusions based on the cases analysed.

B. General legal framework in regard to the convocation of a general meeting on the request of shareholders in Bulgarian non-listed joint stock companies

Under Art. 223, para. 1 of the Bulgarian Commerce Act, the general meeting of a joint-stock company can be convoked by the board of directors (if the company opted for a one-tier system), the managing or the supervisory board (if the company opted for a two-tier system), or on the request of shareholders that have represented at least 5 percent of the capital for a minimum period of three months. The procedure for convoking a meeting at the request of shareholders is detailed in Art. 223, para. 2 of the Bulgarian Commerce Act. This article stipulates that if the request of the shareholders specified is not granted within one month of notifying the company, or if the general meeting is not

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held within 3 months following the notification, the district court shall convoke a general meeting or empower the shareholders to convoke the meeting.

The convocation of the meeting is announced through the issuance of a convocation notice that is published in the commercial register of Bulgaria. However, it is important to note that under Art. 223, para. 3 of the Bulgarian Commerce Act, the statute of the company may stipulate that the convocation can be carried out only by written notices, without announcing the notice in the commercial register. The convocation of a general meeting solely through written notices is not applicable for listed joint-stock companies, however a number of non-listed joint stock companies have opted for this option. As will be analysed below, this has a number of important implications for shareholders.

All joint stock companies keep a shareholder register. The shareholder register contains the full identification of the shareholders, including name, addresses, personal identification number/uniform identification code, and type of shares they own. As explicitly stated in Art. 185, para. 2 of the Bulgarian Commerce Act, a transfer of shares must be entered in the shareholder register to be binding for the company. The shareholder register itself however is not public, and in non-listed joint stock companies, as stipulated in Art. 179, para. 2 of the Bulgarian Commerce Act, it is kept by representatives of the company. The shareholder register is used for determining to whom and to what address to send the respective written convocation notices for general meetings. However, the fact that shareholders themselves do not have free access to the shareholder register, significantly hinders their possibility to effectively send written convocation notices when a general meeting is convened under Art. 223, para. 2 of the Bulgarian Commerce Act.

This is important, as any procedural irregularities can be used as grounds for bringing action for the annulment of the resolutions of the general meeting before the courts. Under Art. 74 of the Bulgarian Commerce Act, all shareholders have standing to bring such action. Furthermore, since the results of certain resolutions of the general meeting need to be entered into the commercial register in order to take effect, lack of written convocation notices also might be considered grounds for refusal to enter such decisions into the register.¹

C. The conflicting approaches of courts in the “Izvor Bottling Company” AD cases:

Some of the most important Bulgarian case law regarding the convocation of general meetings on the request of shareholders concerned a series of cases for the appointment

1 An example to this effect is Decision of the District Court-Shumen dated 10.12.2014, case No. 613/2014, in which a joint-stock company has opted for convocation of general meetings with written notices, without announcement of the convocation notices in the commercial register. In that case, the meeting was convened through a convocation notice announced in the commercial register. The Registry Agency of Bulgaria refused to enter the results of the resolution of the general meeting concerning the appointment of board members, since no proof of sending written notices was presented. The court explicitly stated that if a joint-stock company opts for written convocation notices, announcing the convocation notice in the commercial register is not sufficient.

of new members of the board of directors and the discharge of previous ones in the joint-stock company “*Izvor Bottling Company*” AD.

The factual background of the cases is as follows: “*Izvor Bottling Company*” AD is a joint-stock company incorporated in Bulgaria. The company has issued 51 000 shares. 50 999 of them were owned by the majority shareholder (also a joint-stock company), while the single remaining share was owned by one of the members of the board of directors.

On 29.12.2014, the majority shareholder, by exercising its right under Art. 223, para. 2 of the Commerce Act, was empowered by the Varna District Court to convoke a general meeting on 15.01.2015.² The agenda of the general meeting included the appointment of two new directors and the discharge of one of the existing ones. The member of the board of directors who was to be replaced was the owner of the single share mentioned. It is important to note that Art. 223, para. 5 of the Bulgarian Commerce Act stipulates that the minimum period between the convocation of the general meeting and the publishing or sending the written convocation notice is 30 days. When a general meeting is convoked on the request of shareholders through a court order, the court issues its order specifying the date requested by the shareholder(s). However, in this case, the order was issued less than a month before the date requested by the shareholder. In this case, the shareholder was faced with a dilemma-to submit a new application for a subsequent date, counting on the court to issue its order in a timely manner allowing for legally holding the meeting, or to submit the court order as it was to the commercial register and announce the meeting for a different date, one complying with the minimum 30-day period.

The shareholder chose the latter option, as evident by its application for the announcement of the convocation notice for general meeting in the commercial register.³ In the explanatory notice attached to the application, the majority shareholder stated that despite owning 99,998 % of the shares in the company, the directors of the company did not provide any cooperation in regard to the convocation of the general meeting, thus leaving the shareholder no other option but to convoke the meeting through a court order. However, due to the delay in issuing the court order, the shareholder stated the meeting needed to be announced for a later date that would comply with the minimum statutory 30-day period. The shareholder also stated the meeting was of an urgent nature and the damages of leaving the managers unchanged could be irreparable for the company.⁴ The registry agency complied with the request, and meeting was subsequently held on 20.02.2015, with the majority shareholder adopting the general meeting resolution it proposed.⁵

2 Order number 5003 dated 29.12.2014, case number 1973/2014, Varna District Court.

3 Explanatory Notice attached to Application for announcement of acts No. 20150110220049, submitted before the Registry Agency of Bulgaria.

4 Ibid.

5 Decision 214 dated 05.04.2016, commercial case number 312/2015 of Varna District Court.

Following the 20.02.2015 general meeting, the minority shareholder filed an action for the annulment of its resolutions before the Varna District Court. In Decision 214 dated 05.04.2016, commercial case number 312/2015 of Varna District Court, the court annulled the resolutions of the general meeting, adopting a formalistic and shareholder-unfriendly reasoning. In its decision, the court stated that since the statute of the joint-stock company in question opted for convocation of general meetings through written convocation notices, the announcement of the convocation notice in the commercial register was not sufficient. The court dismissed as irrelevant the arguments of the majority shareholder that it would be unreasonable for shareholders convening a meeting by power of a court order to be required to send written notices to each and every shareholder, as shareholders do not have access to the shareholder register of the company and do not possess information about the addresses of other shareholders. Despite the court dismissing this argument, it stated no potential remedy for this situation.

The court further reasoned that there was no indication that the shareholder convening the meeting has provided written materials about the professional qualifications of the nominated board members, as required under Art. 224, para. 2 of the Bulgarian Commerce Act. The court dismissed as irrelevant the arguments that there was no evidence that the minority shareholder has requested written materials on this subject. Thus, the court adopted a legally formalistic approach that was not based on the way the resolutions of the general meeting were materially affected by the alleged procedural irregularities.

The court also reasoned that the majority shareholder was erroneously empowered by the Varna District Court to convoke the general meeting. In its decision, the court stated that the evidence provided in the proceedings for issuing Order number 5003 of Varna District Court dated 29.12.2014, case number 1973/2014, empowering the shareholder to convoke the meeting, were insufficient, primarily due to the receiver of the request for the convocation of the meeting being referred to solely by his last name in the receipt presented, thus not providing sufficient identification. The court also noted that the shareholder was not entitled to change the dates of the general meeting as provided in the court order, which had been done presently.

The cited Decision 214 dated 05.04.2016, commercial case number 312/2015 of Varna District Court can be criticized as depriving shareholders of the effective opportunity to convoke a general meeting through a court order. First, the decision, to an unreasonable extent interfered with the separately issued court order for the convocation of the meeting. In this new set of proceedings, the court revised the conclusions made in the separate set of proceedings that the company has been properly informed about the request of the shareholder for convening the general meeting. Second, the court offered no remedy for circumstances in which the delay of the court in issuing a court order would result in the illegality of the meeting requested—a problem that is still unresolved in Bulgarian law and

practice. Third, it was evident that the court did not consider the severity of the alleged procedural irregularities in conducting the general meeting, instead considering each and every irregularity sufficient to annul the resolutions adopted.

Perhaps the most problematic aspect of the court's reasoning is the interpretation that if a shareholder company has opted for the convocation of general meeting through written notices, shareholders convoking the meeting through a court order need to send individual written notices to each shareholder. This requirement is unreasonable for a number of reasons. First, as mentioned above, shareholders do not have free access to the shareholder registry of the company. Sometimes, the directors responsible for keeping the shareholder registry might have an incentive not to provide the shareholder registry, for example if the meeting concerns their discharge as directors. Finally, the announcement of the convocation notice in the commercial register fully serves the function of informing shareholders of an upcoming general meeting. The option for joint-stock companies to choose written notices as opposed to announcing the convocation in the commercial register is meant to be facilitate the convocation of the meeting by alleviating the requirement for announcement in the commercial register. It is not meant to be the only legal option for convocation of the meeting.

Following the decision cited, the majority shareholder made a new attempt to discharge the mentioned director and appoint new ones. First, the majority shareholder filed a subsequent request before the courts, requesting to be empowered to convoke the general meeting under Art. 223, para. 2 of the Commerce Act. Its request was granted, with the court empowering it to convoke a general meeting on 13.09.2016.⁶ The general meeting was held on 13.09.2016, and the resolutions proposed by the majority shareholder were adopted. Again, the minority shareholder initiated an action for the annulment of the general meeting resolutions. This time, the action was dismissed by the Varna District Court in Decision 515 dated 21.07.2017, commercial case number 1365/2016. The decision of the court was subsequently upheld by the Varna Appeals Court in Decision number 299 dated 22.12.2017, commercial case number 536/2017. The decision of the Varna Appeals Court was subsequently challenged by the minority shareholder before the Supreme Court of Cassation. In Order number 737 dated 17.12.2018, commercial case number 1418/2018 by the Supreme Court of Cassation, the appeal was not admitted. The order of the Supreme Court of Cassation was final, with no possibility to appeal.

The cited set of decisions adopted a new, more nuanced and reasonable approach. In Decision 515 dated 21.07.2017, commercial case number 1365/2016 by the Varna District Court, the court was presented with arguments almost identical to the ones discussed in the previous set of proceedings. In this case, the convocation notice was also announced in the commercial register. However, this time the court adopted the reasoning of the majority shareholder that when a general meeting is convoked on the request of a share-

6 Order number 2016 dated 13.06.2016, private commercial case number 708/2016, Varna District Court.

holder under Art. 223, para 2 of the Bulgarian Commerce Act, i.e. through a court order empowering the shareholder to convoke the meeting, the convocation notice could be announced in the commercial register. The court explicitly noted that since shareholders do not have access to the shareholder register of the company, they cannot be expected to determine who the current shareholders are and to send the written notices to their addresses.

Perhaps most importantly, the court explicitly stated that when a general meeting is convoked by shareholders, the legality of meeting cannot depend on the actions or the cooperation of the directors of the company. This is due to the fact that shareholders in non-listed joint-stock companies are required to first request the convocation of the general meeting from the directors of the company, and only if this request is not granted, could the court empower them to convoke the meeting themselves. Thus, by definition, the right of shareholders to convoke a general meeting of the company is designed to overcome the inaction of the directors, and cannot be hindered by it.

Furthermore, the court dismissed the complaints of the minority shareholder that he was not provided written materials about the proposed directors. The court noted that the shareholder empowered to convoke the meeting is responsible for the drafting and provision of the written materials to shareholders. In the present case, no irregularity was found, and the court stressed that written materials are provided only if requested by the shareholder.

The Varna Court of Appeals, in its reasoning for upholding the decision, also noted that not every procedural irregularity in regard to the general meeting is sufficient to constitute grounds for annulment.⁷ Instead, the court relied on a functional approach, which analysed whether the alleged irregularity affected the possibility of the shareholder to participate in the general meeting. Thus, for example, despite the general meeting starting at a later hour than the announced in the convocation notice, such irregularity did not prevent the shareholder from voting and thus was not found as grounds for annulment. This reasoning is notable, as it marks an important trend in Bulgarian case law regarding actions for annulment of resolutions of general meetings. Currently, the courts have increasingly began analyzing if the alleged irregularities materially affected the opportunity of the shareholder to participate in the general meeting, rather than considering any irregularity sufficient for annulment of the resolutions.

The final court act in the second set of cases is Order 737 dated 17.12.2018, commercial case number 1418/2018 of the Supreme Court of Cassation. The Supreme Court of Cassation found that the procedural grounds for admitting the case for review were not present, thus the previous decisions entered into force.

7 Decision number 299 dated 22.12.2017, commercial case number 536/2017.

D. Conclusions

The two set of proceedings regarding the joint-stock company “*Izvor Bottling Company*” AD mark two diametrically opposed approaches to the exercise of the shareholder rights regarding the convocation of a general meeting. As evident by contrasting the two sets of proceedings, Bulgarian courts have become less rigid regarding the exercise of the specified shareholder right. This is a positive trend in the field of shareholder protection in Bulgarian non-listed joint-stock companies.