

**COMPANY LAW**

**RIGHTS OF MINORITY  
SHAREHOLDERS**

**FORCED SALE AND FORCED  
PURCHASE**



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##### **1. INTRODUCTION**

Legal protection of minority shareholders includes defining of their position in legislation and accompanying regulations, i.e., the laws governing the rights of companies and the securities market.

Due to the fact that protecting the rights of shareholders greatly affects the quality of corporate governance, it is therefore necessary to determine whether the minority shareholders are provided sufficient protection, whether they use their rights and resources, as well as methods of improving the protection of minority shareholders.

Shareholders' rights in the Republic of Srpska are defined by the Law on Companies<sup>1</sup>, which with the purpose of better protection has been upgraded with the special law that deals with the protection of minority shareholders, i.e., the Law on Takeover of Shareholding Companies<sup>2</sup>.

The legal framework for the protection of minority shareholders and specific forms of privatization have led to a lack of interest of minority shareholders to use all concepts "to fight" with the management of privatized companies.

Bearing in mind that the corporate governance in Bosnia and Herzegovina is at the beginning of its development, the practice is still undeveloped and unadjusted, so the self-regulation and voluntary acceptance of obligations are still at the minimum, i.e. the protection is still achievable by force and under the threat of sanctions by other institutions.

The rights of minority shareholders include a wide range of rights, of which hereby we will discuss only those related to forced sale and forced purchase of shares of minority shareholders. Hereinafter, we will also pay attention to compliance of regulations with

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<sup>1</sup> Law on Companies („Official Gazette of the Republic of Srpska“no. 127/ 08, 58/09,100/11,67/13 )

<sup>2</sup> Law on Takeover of Shareholding Companies („Official Gazette of the Republic of Srpska“ no. 65/08, 92/09, 59/13 )

the European Union, as well as proportion of the rights of minority shareholders that are at their disposal with those that they actually use.

## **2. FORCED SALE AND FORCED PURCHASE**

In our legal system, the Law on Companies introduced relatively new concepts of forced sale (*squeeze-out*) and in parallel with it a concept of protection of the other side – forced purchase (*sell-out*).

The legal nature, as well as a manner of regulating the forced purchase and sale, indicates that there are two approaches to these new concepts.

On the one hand the same can be considered as concepts of company law. Consequently forced purchase and forced sale are regulated by the provisions of the Law on Companies. However, on the other hand the same belong to the area of takeover of shareholding companies and therefore are governed by the provisions of the Law on Takeover of Shareholding Companies.

Opening the issue of conflict of laws, because there are two laws in the same legal system, systematic in the field of economic relations and special related to takeover of shareholding companies, which differently prescribe the percentage of acquiring shares, is therefore avoided with the rapid reaction of the legislator and harmonization of percentage of shares required for the sale or purchase i.e. harmonization of general and special law.

Companies with a small number of free shares are very attractive in the market, therefore, the main motive of a majority owner is just to become the sole owner in order to achieve costs reduction and exit from the stock exchange. In this context, the same uses the right to squeeze out minority shareholders, while the right of minority shareholders is to force the owner to redeem their shares as counterpart to the squeeze out right. The right to sell and the right to purchase are two correlative concepts through which shareholders decide whether to remain in the company and the stock exchange or to abandon it.

### **2.1. Forced purchase/sale of shares**

Forced sale of shares essentially refers to the right of the majority shareholder in the company to force minority shareholders to sell their shares.

According to the Law on Companies, at the proposal of the shareholder who has shares that represent at least 95% of the company's share capital and having at least 95% of the votes of all shareholders possessing ordinary shares (the controlling shareholder)

the Shareholders' Assembly shall decide on forced purchase of all shares of the remaining shareholders.

A person which in the process of a public takeover bid acquires at least 95% of the shares of the target company in accordance with the law governing the securities market in relation to the total number of shares has the right to purchase the shares, to which the public bid referred to, from shareholders who did not accept the sale of shares according to that bid (dissenting shareholder), under the terms of the public bid.

The controlling shareholder is a shareholder who holds shares representing at least 95% of the share capital of the company. A shareholder - the applicant shall state the type, class and number of shares subject to the sale. The application shall be submitted to the joint stock company, and it shall be considered as the same is delivered to the controlling shareholder.

Shares possessed by persons associated with the controlling shareholder shall be considered as shares of the controlling shareholder, provided that such persons are associated with controlling shareholder for a period of at least one year before making a decision on the forced purchase.

According to the Law on Companies, associated companies understands two or more companies in accordance with this law, which are mutually associated in the following way:

1. Participation in the share capital or general partnership interests (*companies connected by share capital*)
2. With a contract (*companies connected with a contract*) and
3. With both share capital and contract (*mixed connection of companies*).

Due to the fact that the Law on Companies relates this concept only to the acquisition of share participation in the takeover of joint stock companies, a question arose whether the concept of forced sale can also apply to numerous other cases of "forced squeeze out of minority shareholders" when the majority shareholder acquired prescribed threshold of participation for this concept. The absences of appropriate practices, new concept, or lack of voluntary application are just some of the reasons in favour of a very restrictive interpretation of this concept.

The Articles of Association may provide that the forced purchase is not allowed or may provide a higher percentage of participation for the purchaser in the share capital as a condition for the forced purchase.

A shareholder who in the public takeover bid gave to shareholders of the target company the right to choose between compensation in cash or in securities or other forms of assets, this right must give to the dissenting shareholder in a written form.

In order to achieve the right to forced purchase the purchaser shall send a written application to minority shareholders no later than 120 days from the deadline of the public offering, indicating the terms of purchase of shares from the public bid, while a copy of such application should be referred to the management board of the target company.

If a shareholder does not receive a response on acceptance of the application for forced sale within 30 days of the submission of the application, then is entitled to send a notice to the target company on redemption of shares of dissenting shareholder and pay compensation to the company or handover other forms of assets from that application with the authorization that the compensation or other forms of assets shall be transferred to the dissenting shareholders.

Upon receipt of a written notice the target company is obliged to enter the bidder in the Central Registry as shareholder of forcibly redeemed shares, as well as in the court register in accordance with the law governing the registration of business entities while received remuneration shall be held in its own name on behalf of minority shareholders, until the same is transferred to that shareholder.

An essential element in exercising the right to the forced sale is pricing, where the price shall be determined according to the market value of the shares on the day that is not preceded by more than three months to the day of the decision on the forced sale, without taking into account its expected increase or decrease as a result of the decision on forced sale. In this regard, the controlling shareholder shall determine the amount of compensation which is to be paid to minority shareholders.

When determining the amount of compensation the controlling shareholder is obliged to take into account material and financial status of the company at the time of the decision adoption at the Shareholders' Assembly, while the authority in charge of managing the company is obliged to submit to the controlling shareholder all available documentation and provide all information needed in relation to the determination of the amount of the compensation.

## **2.2. Forced purchase of shares**

The forced purchase of shares is related to the rights of minority shareholders to compel the majority shareholder to purchase their shares. The obligation of purchasing shares from the minority shareholder is of a cogent nature and the controlling shareholder is obliged that at the written request of minority shareholder purchase his shares under the prescribed terms.

According to the Law on Companies, the concept of forced purchase is not related to the method of acquiring majority participation in the share capital of the company, but

it gives an opportunity to minority shareholders that from the shareholder who acquired 95 % of interest in the company within prescribed deadlines and in prescribed manner request purchase of their shares.

A minority shareholder may submit a request to the majority shareholder no later than six months from the date of acquisition of the majority package. The majority shareholder is required no later than 30 days from the date of receipt of the request for forced purchase to send a written response to that request.

The controlling shareholder determines the amount of compensation to be paid to minority shareholders. The price of shares by which the controlling shareholder is obliged to purchase the same shall be determined by appropriate application of the rules of Law, the price of shares to be paid to the dissenting shareholders and all in a way that as relevant shall be consider the price of the last share by which the same acquired 95%.

In addition to the amount of compensation shall be calculated the default interest accrued from the registration of the decision on the transfer of shares to the controlling shareholder until the date of payment to the minority shareholders. The Company shall determine the price of these shares within 60 days of receipt of the request and shall inform about it the controlling shareholder, within the same deadline, where the same is obliged that within a period of 30 days, pay the specified amount.

The forced purchase shall be registered in accordance with the law governing the registration of business entities and shall be registered in the Central Registry in accordance with the law governing the securities market.

In the event that the offered compensation is not appropriate, each minority shareholder may, within 30 days from the date of registration of the decision on the transfer of shares of the controlling shareholder in the court register, propose to the court that in an extrajudicial procedure determines appropriate compensation. The same right belongs to the minority shareholder if the controlling shareholder did not pay the compensation properly (without calculating the interest, or did not pay the full amount, etc.), or in the case if the controlling shareholder did not offer (within 30 days after receiving the request of any of the remaining shareholders) an adequate financial compensation for shares of the individual minority shareholder.

The right to the payment of the compensation shall be valid for three (3) years from the date of the registration of the decision on the transfer of shares in the court register, after which the funds, which were deposited in the name of financial compensation, shall be transferred to the Budget of the Republic of Srpska.

### **3. FORCED PURCHASE AND FORCED SALE IN THE TAKEOVER PROCESS**

It is very important to make a difference between the forced purchase and forced sale, which are regulated by the Law on Companies and the Law on Takeover of Shareholding Companies.

The restructuring of the ownership structure through takeover of joint stock company techniques may place the minority shareholders in a very unfavourable position. Takeover of joint stock companies is subject to special regulations with an aim to ensure equality of shareholders and protection of minority shareholders on the basis of the Law on Takeover of Shareholding Companies.

The basic mechanism of protection of shareholders as prescribed in this law is reflected in the mandatory public takeover bid, which must meet the prescribed requirements. Accordingly, the acquirer must within the prescribed period inform the issuers and the Commission for Securities of the decision on the takeover, and publish the decision in at least two printed media, and within eight days from the publication of the decision shall submit the request for approval of the public takeover bid.

The bidder, as well as persons acting jointly with the same, which after the takeover bid acquire 95% of the total number of votes is obliged that at the written request of the remaining shareholders (minority shareholders) purchase their shares at the price of the takeover bid.

The request for the forced purchase of shares a minority shareholder may submit within 90 days of the expiry of the takeover bid.

If the bidder, or a person acting jointly with the same, up to the date of the application of the minority shareholder acquired shares of the issuer at a price that is higher than the bid price, then is obliged to buy from the minority shareholder the remaining shares at the higher price.

The bidder, as well as persons acting jointly with the same, is obliged to purchase shares of minority shareholders within 30 days from the day of receipt of the request of minority shareholders. Along with the application for transfer of ownership rights on the shares subject to the forced purchase in the process of takeover it is necessary to attach the request of the minority shareholder for forced purchase of shares addressed to the bidder, the sale-purchase contract of shares, bank certificate on executed payments of the share price as well as other documents prescribed by the applicable regulations of the Central Registry.

The Central Registry of Securities shall, upon completion of the transfer of shares to the name of the bidder, publish on its website the appropriate notification containing general information on the issuer that has been the subject of takeover, the name and

surname of the person whose shares have been forcibly sold, number of forcibly sold shares for every person, the price per share established in the bid and an indication of the rights and obligations of persons whose shares were forcibly sold.<sup>3</sup>.

Notice regarding transfer of shares the Central Registry shall deliver to the Banja Luka Stock Exchange, stockbrokers and issuer.

#### **4. FORCED PURCHASE AND FORCED SALE BASED OF THE EUROPEAN UNION DIRECTIVES**

The right of the majority shareholder to force minority shareholders to sell their shares (forced sale), as well as the complementary right of minority shareholders to require from the majority shareholder to purchase their shares (forced purchase), are two legal concepts that were not regulated at EU level until adoption of the EU Directive on Public Takeover Bids (EU Directive on Takeover).

Despite the legal separation, forced sale and forced purchase, economically speaking form one unit. According to the decision of the EU Directive on Takeover, there must be a direct or indirect link between the right to a forced sale or forced purchase, and complete public takeover bid. In both cases there is a principle that certain equity-participation must be acquired as a result of the successful acquisition of a public offering.

Accordingly, the EU Directive on Takeover redirected the domain of application of forced sale and forced purchase to the field of the takeover, leaving it on states to decide on the acquisition of equity participation threshold of the voting shares, provided that the range of 90% -95% of that participation should be determined.

#### **5. CONCLUSION**

Once the bidder acquires 95% of shares of the target company, as a result of the public takeover bid, then shall be applied a rule on the forced purchase according to the Law on Takeover of Shareholding Companies. However, in all cases where a person acquires 95% of shares in another company, provided that this percentage is not reached in the takeover, the majority shareholder shall be obliged to purchase shares of the remaining shareholders at their request, according to the rules of the Law on Companies. Hence, it can be concluded that the forced purchase is a general concept of the company law, and in this respect our law follows the modern European tendencies in this area.

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<sup>3</sup> Instruction on the manner of exercise of the rights to forced sale and purchase in the takeover process ( „Official gazette of the Republic of Srpska“ no. 65/08 and 92/09)

Namely, initially there were more than 1 million of the minority shareholders in Republic of Srpska. Today, in the Republic of Srpska in investment funds there are more than 450,000 of minority shareholders, while there is over 280,000 of minority shareholders in over 600 joint stock companies listed on the Stock Exchange.

If there is an improvement of the position of minority shareholders, and if they are allowed to exercise the rights guaranteed by the law, then the situation in the companies would be improved and the same would generate higher incomes, then demand would be enlarged, and consequently it would lead in favour of the development of entrepreneurship, and the economic prosperity of the Republic of Srpska.

Comparative analyses showed that our laws do not differ much from the European law, but quite often it happens that the issues prescribed by laws are not present in practice. Because of this discrepancy between the law and reality, assets and shareholders' rights derived therefrom are practically unprotected. Terrain of voluntary implementation is not yet sufficiently applied in practice, so the basic protection is provided by compulsion, through courts and regulatory authorities such as the Commission for Securities.

On the list of the WEF (World Economic Forum) global competitiveness, when it comes to protecting the rights of minority shareholders, Bosnia and Herzegovina is at 130th place out of 148.

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