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THE NATURE OF INVESTIGATION PROCEEDINGS OF LEGAL ENTITY UNDER THE CIVIL CODE OF LITHUANIA

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Abstract. *With reference to the Dutch model, which has been adopted by the Lithuanian Civil Code, the possibility to renounce Investigation Proceedings in the Articles of Incorporation or shareholder agreements is analysed in this article. The mandatory nature of the Investigation Proceedings is derived from the provisions of the Code, mainly: from an active role of the court, typical to the cases with the element of public interest, from specific rules for protecting the public interest in the course of the Investigation Proceedings, also taking into account statutory duties of managers, the scope of which may not be narrowed by SHA, and the fact, that the Investigation Proceedings is generally designated to be an instrument to safeguard the interests of minority shareholders against the abuse of their rights by the company, and, finally, acknowledging the extraordinary nature of remedies available in the Investigation Proceedings.*

Keywords: *investigation proceedings, company law, rights of minority shareholders, shareholder agreements*.

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Introduction

Lithuanian company law has been employing a legal instrument, known as Investigation activities of legal entity (as it is set forth in the Articles 2.124 – 2.131 of the Civil Code of the Republic of Lithuania) for a decade. This instrument became a well- known measure to monitor the management of legal entity. In this type of litigation the interests of the shareholders are at stake, the question of possibility to renounce the application of the Investigation Proceedings in Articles of incorporation of the company or (and) in shareholder agreements should be validly raised. In this article I will focus only on the Investigation Proceedings of the company, although, technically all types of legal entities (excluding only State, municipalities, and religious communities) may be subject to this legal instrument.

Doctrine. No research on the issue is available in Lithuania. The main sources are the Articles 2.124 -2.131 of the Civil Code (Further on CC) and a short outline in the Commentary on the Civil Code (8 pages in length)[1], published immediately after the Civil Code came into effect. The Commentary was intended to define in general terms the content of regulation. Due to its chronology it fails to give an overview of the present situation. However, Commentary significantly affects national case law with the Lithuanian courts repeating the text of the Commentary practically word-for-word in their rulings and judgements.

Case law. The Civil Code has been in effect only for ten years; consequently, existing case law is not exhaustive, and in many instances the courts do not have an opportunity to address certain problematic issues of the Code or only deal with these matters indirectly. Moreover, the role of court rulings as a source of law is mixed - Lithuania uses the civil law system. However, the Constitutional Court[2] has held that courts must ensure uniform application of the law in the courts of all instances and the duty of the Supreme Court to ensure uniform application of law is expressly stated in the Law on Courts. Notwithstanding, uniform and comprehensive case law is still an objective. Certain relevant issues of Investigation proceedings have been examined by the Lithuanian courts more than once (such questions as whose actions may be subject to the investigation and court's discretion to select a remedy) and the case law on these matters is comprehensive; other matters concerning these sections of the Code have not been subject to any judicial analysis whatsoever or where an attempt at an analysis has been made, the court's arguments are only fragmentary and may not be considered as reflecting the existence of uniform case law.

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1 *Lietuvos Respublikos civilinio kodekso komentaras. II Knyga. Asmenys* [The Commentary of the Civil Code of the Republic of Lithuania. Book II. Persons]. Mikelėnas, V.; Bartkus, G., *et al*., Vilnius: Justitia, 2002, p. 247−254.

2 Ruling of the Constitutional Court of the Republic of Lithuania on the compliance of sub-paragraph 2 of paragraph 1 of Article 62, paragraph 4 (wording of 11 July 1996) of Article 69 of the Republic of Lithuania Law on the Constitutional Court and paragraph 3 (wording of 24 January 2002) of Article 11, paragraph 2 (wording of 24 January 2002) of Article 96 of the Republic of Lithuania Law on Courts with the Constitution of the Republic of Lithuania, dated 28 March 2006. *Official Gazette*. 2006, No. 36-1292.

The jurisprudence of other countries: The Dutch Civil Code and doctrine. The drafters of CC (namely G. Bartkus, Lithuanian drafter of the regulation on legal entities in CC), in the Commentary of CC, which in terms of its authority is crucial in establishing the doctrine of Investigation Proceedings in Lithuania, notes that the instrument of the Investigation Proceedings have been acquired from the Dutch Civil Code.[3] Lithuania has adopted the rules of the inquiry proceedings (the term for Investigation Proceedings used in Netherlands) without any significant modification; thus, the regulation of Investigation Proceedings in both Lithuania and the Netherlands is very similar.[4] Therefore, aiming to disclose the policy of Lithuanian law makers, I will rely on the Dutch doctrine and case law.

1. Nature of Investigation Proceedings of the Company

There are two possible viewpoints to the question on the nature and purpose of the Investigation Proceedings:

Non-mandatory nature of Investigation Proceedings. The Investigation Proceedings are designated to safeguard exclusively private interests of shareholders through the measures of control for proper management; therefore, the shareholders may waive the right to initiate the proceedings in the Articles of Incorporation and/or the Shareholders' Agreement; or

Mandatory nature of Investigation Proceedings. The Investigation Proceedings is aimed at safeguarding the interests of all stakeholders of the company through the measures of control for proper management. This instrument is implemented through shareholders, but as it serves to protect broader interest, therefore can't be excluded or modified in the Shareholders' Agreement.

From my viewpoint, the second statement is correct for the reasons that follow below.

2. Policy Goals of Investigation Proceedings

The direct purpose of the Investigation Proceedings is to analyse on request of the shareholders whether the company is being managed according to the legal standards and to eliminate deficiencies by using the measures that can be employed by the court. The case law of the Lithuanian courts, without diverging from the text of the Commentary, has emphasized that improper activities of a legal person mean improper activities of the management bodies and/or the members of the management bodies of a legal person. According to the LSC, such improper activities should be understood as an infringement

3 The Commentary of the Civil Code of the Republic of Lithuania, *supra* note 1, p. 247.

4 For further comparison, see the Dutch Civil Code. Undoubtedly, there are differences, e.g. the Dutch Civil Code provides for the cost appropriation scheme, and the right of trade unions to initiate an investigation, but the fundamental provisions are analogous.

of the provisions of articles 2.86 to 2.87 of CC.[5] Aforementioned provisions deal with the statutory duties of the members of the management bodies. These duties are fiduciary by nature (loyalty, good faith, confidentiality, no conflict of interest) and neither can be excluded nor modified by shareholders.

For establishing in the Investigation Proceedings whether the management is proper, on the ground of the experts' findings and conclusions, the court assesses whether the management bodies have violated their statutory duties to the legal person. The answer to this question will largely depend on the concept of a company employed by the court – whether the company is supposed to represent only the interests of the shareholders or is obliged to take into account the broader interests of all stakeholders.

Even if one was to follow the concept that the company has to represent exclusively the interests of the shareholders, it could not be assumed that the company's interests coincide exclusively with the interests of a majority shareholder, and directors properly perform their duties by representing solely the major shareholder. The interests of minority and majority shareholders are often not homogeneous, and directors have to take into account those diverse interests. Furthermore, if we assume, that the proper performance of duties by management bodies has to be in the conformity with the interests of all stakeholders (shareholders, employees, creditors) it would be even more complicated to define the requirements for proper management. As a matter of fact, not only the shareholders as direct beneficiaries, but also other interest groups, i.e. employees and creditors, are interested in proper management of the company and its continuity. To a certain extent, it is even within the public interest to avoid ceasing the operation of the company as a result of improper management. Therefore, for more than a decade, the case law in Lithuania recognises that the duties of directors arise to the company as an entity with separate interests other than that of the majority shareholder,[6] and in some cases these duties arise to third parties, particularly creditors.[7]

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5 The propriety of the management of the legal entity is assessed based on the proper performance by the members of management bodies of their duties prescribed in Articles 2.86 to 2.87 of the Civil Code as construed by the uniform case law of the Supreme Court of Lithuania. See the following rulings of the panel of judges of the Civil Division of the Supreme Court of Lithuania: the ruling of 11 February 2008, Case No. 3K-3-73/2008;

6 See the ruling of the Civil Division of the Supreme Court of Lithuanian of 29 March 2000 in civil case No. 3K-3-383, Cat. 45; *Teismų praktika*, 14.
"The company and its management bodies are linked by fiduciary relationships, i.e. relationships based on mutual trust; therefore, all the management bodies of the company must operate exclusively in the interest of the company. A management body of the company must vote against any decision contrary to the interests of the company. In cases where a member of the management body of the company is also a shareholder of the company, his interests as the shareholder and as the member of the management body of the company may differ. The interests of the company and of its shareholders may also vary. In the event of a conflict of interests, the principles of good faith, fairness and prudence require a member of the management body of the company to notify other management bodies of the company in this regard. However, personal interests, whatever they may be, do not release the member of the management body of the company from his fiduciary duty to act exclusively in the interest of the company."

7 The cassation court's position is that civil liability of the head of the company may arise both to the company where the head of the company acts contrary to the interests of the company and to third persons where the

2.1. Investigation Proceedings – the Mechanism of Resolution of Conflicts between Shareholders?

The mere fact that a shareholder may initiate an investigation of the company's activities does not reduce the Investigation Proceedings to the mechanism of resolution of conflicts between shareholders. This *sui generis* instrument is designed not only to protect direct private interest of shareholder, but also "public" interest of the company, both that of individual shareholders and of other stakeholders. Dutch lawyers are of the same position stating as follows: "*The inquiry proceedings can also be seen as a typical Dutch product in the sense that it is not an instrument whose use is limited to the shareholders' benefit. Others may also demand the initiation of an inquiry, making it more or less an instrument for the public welfare. The plaintiff cannot claim for damages through the inquiry proceedings. At the end of the proceedings he can only request measures which are purported to further the interests of the company*.[8]"

Statutory framework: Though the Civil Code does not provide *expressis verbis* that the right to initiate an Investigation Proceedings is of mandatory nature, both the language of the Civil Code, which makes no such exclusion, and the abundance of rules for protecting the public interest justify the assumption that the right to Investigation Proceedings is imperative.

The legislature's intent to make the instrument of Inquiry Proceedings non revocable in SHA, is supported by the fact, that the norms of the Investigation Proceedings were adopted from the Dutch Civil Code, in which the mandatory nature of inquiry proceedings is quite clear. The provisions of the Dutch Civil Code designated to regulate the shareholder's right to initiate an inquiry proceedings *are mandatory:* "Its mandatory nature derives from art. 2:25 of Dutch CC which states that the provisions of Book 2 only may be modified to the extent allowed by the specific provision."[9] The provisions stipulating the inquiry proceedings, however, do not provide for any exclusions (see the Dutch Civil Code, Book 2, Articles 344 to 359), thus a general rule of imperativeness is applicable to the Inquiry Proceedings.

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head of the company violates the restrictions establishing certain guarantees of such persons (the ruling of an expanded panel of judges of the Civil Division of the Supreme Court of Lithuania, dated 25 May 2006, in civil case *K. J. J. v. V. K. et al.*, case No. 3K-7-266/2006; the ruling of the Civil Division of the Supreme Court of Lithuania, dated 5 May 2011, in civil case No. 3K-3-228/2011.

8 See Timmerman, L.; Doorman, A. Rights of minority shareholders in the Netherlands. *A report written for the XVIth World Congress of the International Academy of Comparative Law*, p. 55 [interactive]. [accessed on 2012-04-23]. <http://rechten.eldoc.ub.rug.nl/FILES/root/Algemeen/Recht9/2005/rightsminority/minorityshh. pdf>.

9 Meinerna, M. Mandatory and Non-Mandatory Rules in Dutch Corporate Law. *Electronic journal of comparative law*. 2002, 6.4: 3−4 [interactive]. [accessed on 2012-04-23]. <http://wwwejcl.org/64/art64-10.htrnl>.

3. The Features of Investigation Proceedings that Reveal Mandatory Nature of the Instrument

1) The Investigation Proceedings is an instrument for safeguarding the rights of minority shareholders. It is non-revocable right of minority shareholders to initiate the Investigation Proceedings[10]. In the doctrine, the instrument of Investigation Proceedings is widely presented as a measure for protecting the rights of minority shareholders.[11] In Lithuania, the shareholders or a group of shareholders holding or managing no less than 1/10 of the shares may initiate the proceedings. The right of minority shareholder to initiate the Investigation Proceedings is inherently connected with the protection of public interest. Furthermore, the Constitutional Court has held the protection of the rights of minority shareholders is a public interest[12], the same position was upheld by LSC[13], and therefore any arrangement restricting the rights of minority shareholders would likely be recognised as inherently contrary to public policy and thus void.

2) Investigation Proceedings are designated to protect public interest. Paragraph 2 of article 2.125 of the Civil Code provides that the public prosecutor, in an attempt to safeguard public interests, including in cases where the activities of a legal person, its management bodies or the members of its management bodies are contrary to the public interest, shall have the right to apply for the investigation of activities of a legal person. This provision was transposed almost word-for-word from the Dutch Civil Code; therefore, in the absence of cases initiated by the public prosecutor with regard to the Investigation Proceedings in Lithuania, an overview of the concept of the public interest recognised in the practice of Dutch courts is presented. Dutch lawyers recognise that "*The phrase 'public interest' is hard to define. In the Nedlloyd inquiry (OK 30 March 1989, NJ1990, 176 and HR 5 September 1990, NJ 1991, 62), the Supreme Court*

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10 **Article 2.125. Persons Enjoying the Right to Apply for Investigation of Activities**
1. The following persons shall enjoy the right to apply for investigation of activities:
1) one or several shareholders who hold or manage shares the par value of which accounts for no less than 1/10 of the authorised capital;
2) one or several members of a partnership whose interest accounts for no less than 1/10 of all interest;
3) one or several members of a farming partnership or a co-operative society (co-operative) whose member shares account for no less than 1/10 of all member shares;
4) members of a legal person, other than members of legal persons listed in Articles 2.35 and 2.37 and in sub-paragraphs 1, 2 and 3 of the given paragraph, who have no less than 1/5 of all votes;
5) persons as well as members of a legal person who, according to incorporation documents or contracts concluded with legal persons, have been granted the said right.
2. The public prosecutor shall also have the right to apply for the investigation of activities of a legal person in an attempt to safeguard public interests, including the cases where the activities of a legal person, its management bodies or the members of its management bodies are contrary to the public interest.

11 Andenas, M.; Wooldridge, F. *European Comparative Company Law*. Cambridge University Press, 2006, p. 374.

12 See the ruling of the Constitutional Court of the Republic of Lithuania of 17 January 2006 in case No. 25/04 "On the compliance of the Republic of Lithuanian Law on Securities Market <...>". *Official Gazette*. 2006, No. 8-284.

13 See the ruling of the Civil Division of the Supreme Court of Lithuanian of 4 June 2003 in civil case No. 3K-3-650.

decided that a 'specific public interest' is required, to be decided on the basis of facts and circumstances. This implies that more general and important interests, surpassing purely individual interests, may be harmed. This means that the advocate general is not free to transform any individual interest into a public interest and that not every act in conflict with private law automatically conflicts with the public interest. Circumstances that may make an interest a public interest include when the continuity of a large company is in danger (HR 10 January 1990, NJ 1990, 466), when there is a serious threat to employment (OK 28 December 1981, NJ 1983, 25), when the reliability of the (public) annual accounts is in danger (OK 7December 1989, NJ 1990, 242) and when there are strong suspicions of criminal behaviour (OK 17 March 1983, NJ 1984, 462)."[14]

The aforementioned concept of the public interest clearly shows that the goal of the Investigation Proceedings is not to protect the interest of an individual shareholder. The interest of an individual shareholder may even be contrary to a general interest to safeguard the continuity of a company[15], but in the Investigation Proceedings only the latter is actually protected.

3) The restrains on principle of party autonomy in Investigation Proceedings. The Investigation Proceedings have two independent stages, the first of which the shareholders may initiate without seeking the use of remedies provided in the second stage. The two independent parts are as follows: recognition of unlawful actions, the fact of improper management (declaratory judgement)[16] and the imposition of measures referred to in Article 2.131 of the CC[17]. The inquiry proceedings in the Dutch law also have two independent objectives: firstly, to investigate factual situation in the company

14 Asser-Van der Grinten-Maeijer, 2- III, No. 524 translated and cited in Timmerman, L.; Doorman, A., *supra* note 8, p. 58.

15 This includes cases where a company is part of a vertically integrated undertaking, and controlling shareholders may generate economic benefits through other companies of the group and (or) only externalise risks in a particular company.

16 See paragraph 4 of Article 2.126 of the Civil Code. Upon the receipt of an application and having heard the reasoning of the parties, the court shall pass a judgment on the investigation of activities of the legal person if there are grounds to presume the feasibility of circumstances specified in Article 2.124, paragraphs 2 and 3 of Article 2.125 of this Code, <...>. Paragraph 1 of Article 2.130 of the Civil Code provides as follows: Having received the experts' report and recommendations, the court shall notify the parties and their representatives thereof and send copies of the experts' report and recommendations to each party and their representatives as well as convene a court hearing for discussing the experts' report and recommendations.

17 **Article 2.131. Measures Applied by the Court**

1. <...> [T]he court may <...> apply one of the following measures:
   1) to revoke the decisions taken by the bodies of the legal person;
   2) to suspend the powers of the members of the management bodies of the legal person or to exclude a person from the members of the management body;
   3) to appoint provisional members of the management bodies of the legal person;
   4) to authorise non-implementation of certain provisions of incorporation documents;
   5) to direct to amend certain provisions of incorporation documents;
   6) to temporary transfer the voting right vested in the member of the management body of the legal person to another person;
   7) to direct a legal person to take or not to take certain actions;
   8) to liquidate a legal person and to appoint a liquidator. <...>

and to establish the person responsible for improper management (a backward-looking aspect) and secondly, to impose the measures that would allow for the substantial improvement of the entity's management (a forward-looking aspect)[18]. Thus, a claimant may only request to establish the fact of improper management without requesting for the application of any additional remedies. As a matter of fact, in majority of Dutch cases, claimants request not only to recognise the existence of unlawful actions, but also to apply a specific remedy; however, there are the cases where a declaratory ruling is merely demanded.[19] In Lithuania, all present cases on the Investigation Proceedings have both stages; nevertheless, the Civil Code provides for the possibility of applying only the first stage. In certain cases, where the statute of limitations for the annulment of decisions of the legal entity has expired, there is no other option but to recognise the fact of commitment of improper actions if the director that passed the decisions is no longer employed in the company[20]. A shareholder may pursue a declaratory judgement seeking prima facie evidence for use in an action against directors under tort law. The fact that in the investigation proceedings, the court may declare that an unlawful action was committed and not apply a remedy shows that the role of the court in these proceedings is to ensure the balance between the interest groups of the legal person (stakeholders) and not to protect a specific interest of a shareholder.

Furthermore, an advance dispute settlement procedure under paragraph 2 of Article 2.126 of the Civil Code, providing that an application may be filed only if the claimant has applied to the legal entity requesting to terminate improper activities and has provided a reasonable time limit to eliminate the circumstances, as well as the requirements for the content of the application (a referral, which either fails to specify improper activities or improper discharge of duties or to give reasons why the activities are considered to be improper, shall not be deemed to be an application), show that in this respect, a major concern of the court is to avoid possibly disturbing the activities of the company, unless a reasonable ground exists, and to protect the shareholder's interest to the extent it does not conflict with the general interest of the company.

3.1. An Active Role of Courts in Investigation Proceedings

In Lithuanian civil proceedings, the court takes an active role in cases related to the protection of the public interest[21]. The court actively participates in the Investigation Proceedings, enjoying wide powers of discretion, and adversarial principle of party autonomy in such cases is not applied to full extent. Practically, claimants may initiate an investigation, but they may not affect its course. Furthermore, they may determine the scope of the investigation and remedies only to a very limited degree. Wide discretion of the court manifests in all stages of the Investigation Proceedings. Firstly, the court

18 Timmerman, L.; Doorman, A., *supra* note 8, p. 56.

19 *Ibid*., p. 56.

20 The Commentary of the Civil Code of the Republic of Lithuania, *supra* note 8, p. 254. In addition, the ruling of the Civil Division of the Supreme Court of Lithuania of 9 December 2008 in civil case No. 3K-3-590/2008.

21 E.g., Article 144, paragraph 2 of Article 179 of the Code of Civil Procedure.

decides where there is a sufficient ground to start an investigation; secondly, the court defines the limits of the investigation, which may to some extent vary from the grounds specified by the claimant; thirdly, the court imposes remedial measures (technically, only when the claimant requests) but it is not bound to impose the remedy indicated in the statement of claim.

The wide discretion of the court to initiate or to refuse to initiate an Investigation Proceedings, if, from the court's perspective, there is no sufficient information that the activities of the legal person are improper, shows that the legislator sought to protect the legal entity from the shareholders' unreasonable intention to interfere in the activities of the legal person (paragraph 4 of Article 2.126 of the Civil Code).[22] The case law of SCL also justifies this position: SCL repeatedly states, that in each case, the court has to determine whether there are circumstances that warrant the investigation of activities of a legal person, its management bodies or the members of its management bodies. The facts alleged by the claimants are for court assessment purposes only. In assessing the circumstances, the court does not examine or evaluate specific activities of a legal person, its management bodies or the members of its management bodies. The court only decides whether the alleged facts in the application constitute the ground for initiating the investigation or states that the indicated circumstances constitute no ground for initiating the investigation and rejects the application[23].

The wide discretion of the court to establish the scope of the investigation. The entire structure of the Investigation Proceedings shows that claimants are not fully entitled to restrict the court's right to establish the scope of the investigation activities, as it would be anticipated in commercial dispute. The right to initiate an Investigation Proceedings is vested in the persons who, due to their status in the company, often do not dispose of detailed information about the activities of the legal entity, i.e. the owners of 10 per cent of its shares, who are underprivileged to access all internal documents of the company under the Law on Companies[24], as well as the public prosecutor. Therefore, it is practically impossible for such claimants to properly foresee the scope of the investigation in advance. They have to only justify the seriousness of their doubt

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22 Paragraph 4 of Article 2.126 of the Civil Code of the Republic of Lithuania. Upon the receipt of an application and having heard the reasoning of the parties, the court shall pass a judgement on the investigation of activities of the legal person if there are grounds to presume the feasibility of circumstances specified in Article 2.124, paragraphs 2 and 3 of Article 2.125 of the Code, or shall reject the application.

23 The ruling of the Civil Division of the Supreme Court of Lithuania of 9 December 2008 in civil case No. 3K-3-590/2008.

24 **Article 18 of the Law on Companies. Shareholder's Right to Information.** 1. A company shall, at a shareholder's written request and within 7 days from the receipt of the request, grant to the shareholder access to and/or submit to him copies of the following documents: the Articles of Association of the company, sets of annual financial statements, annual reports of the company, the auditor's opinion and audit reports, minutes of the General Meetings of Shareholders or other documents executing decisions of the General Meetings of Shareholders, the recommendations and responses of the Supervisory Board to the General Meetings of Shareholders, the lists of shareholders, the lists of the members of the Supervisory Board and the Board, also other documents of the company that must be publicly accessible under laws as well as minutes of the meetings of the Supervisory Board and the Board or other documents executing decisions of the above-mentioned company bodies, unless these documents contain a commercial (industrial) secret of the company, confidential information.

that the activities are improper, rather than to specify any particular actions that should be examined. The court, being convinced of the validity of this doubt and having considered the benefit and damage of the investigation to a company, shall assign the investigation on propriety of management activities to experts who enjoy very wide powers. Thus, the possibility of the parties to the proceedings to affect the investigation by experts is limited to a minimum. Furthermore, a systematic analysis of paragraph 2 of Article 2.126 of the Civil Code (requiring the claimant in his application to flesh out *only* how the improper activities of the legal person are manifested and to specify the grounds why the activities are improper), paragraph 4 of Article 2.126 of the Civil Code (providing that the court, having considered all the circumstances, must adopt a ruling on the investigation of activities of a legal person or deny investigation), and Article 2.128 of the Civil Code (listing the very wide powers of experts) reveals that the court may enjoy wider powers in establishing the scope of the investigation than in a commercial dispute and may interpret the required scope of investigation and grounds listed in the application rather extensively[25].

The wide powers of the court to apply remedies. The SCL in its case law has directly addressed the correlation between paragraph 2 of Article 265 of the Code of Civil Procedure (the court's obligation not to exceed the scope of the claims filed by the parties) and Article 2.131 of the Civil Code (i.e. the court's right to select the measures in the final stage of Investigation Proceedings). The case law of the Supreme Court of Lithuania is as follows: the parties' request of the particular measure does not limit the court's discretion to select most efficient measure. This SCL position, that the court is not bound by the applicant's request, is consistent and uniform.[26]

3.2. Inherent Public Interest Element in Investigation Proceedings

Special jurisdiction is provided for the cases of this type, i.e. regional courts are the courts of first instance for Investigation Proceedings(paragraph 7 of Article 27 of

25 The ruling of the Civil Division of the Supreme Court of Lithuania of 28 June 2010 in civil case No. 3K-3-299/2010: *The panel of judges notes that the referral of V. A., dated 26 April 2006, (Vol. 1, file pages 139-143) shows that not only the circumstances specified in the appellants' cassation appeal, but also the reasons of unprofitability of UAB Ad Locum, the compliance of the activities of the company's manager with the requirements of Article 2.87 of the Civil Code fall within the scope of this case on the investigation of activities of the legal person. As requested by the court, the expert examined all reasons of unprofitability of the company and arrived at a reasonable conclusion. The court of appellate instance, having examined the evidence collected in the case concerned, obtained a reasonable basis for the conclusion that the court of first instance had properly established the subject matter and the scope of the case and had ruled without violating the ban to exceed the claims filed in the case (paragraph 2 of Article 265 of the Code of Civil Procedure).*

26 The ruling of the Civil Division of the Supreme Court of Lithuania of 7 February 2005 in civil case No. 3K-3-16/2005; *the SCL has pronounced more than once on the application of the provisions of Article 2.131 of the Civil Code: the panel of judges notes that pursuant to paragraph 1 of Article 2.131 of the Civil Code, the court, having established that the activities of the management body of the legal person were improper, may apply one of the measures listed in paragraph 1 of this Article. In applying the measures provided by law, the court is not bound by the application of the claimant.* The ruling of the Civil Division of the Supreme Court of Lithuania of 28 June 2010 in civil case No. 3K-3-299/2010.

CCP) and participation of an advocate is mandatory (paragraph 3 of Article 2.126 of CC). Furthermore, in the course of the investigation, the court, at its own initiative, is obliged to take actions necessary to safeguard the public interest. For example, the court has a duty to send the experts' report and recommendations to the respective public institutions, which exercise the supervision of activities of a legal person (paragraph 2 of Article 2.130 of CC). The court role is analogous only in the cases with the element of protection of the public interest, i.e. cases involving employment (Article 414 of CCP), public procurement (Article 423^8 of CCP) and family matters (Article 376 of CCP).

3.3. The Parties to Investigation Proceedings

Parties to the dispute - by definition, shareholder (or the public prosecutor protecting the public interest) (the claimant) and a legal entity (the respondent) are the parties to the Investigation Proceedings. If the public prosecutor initiates the investigation, the status of the beneficiary, in whose interests the proceedings are initiated, is a third person without independent claims (Article 49 of the CCP).

As a matter of fact, the practice of Lithuanian courts in this respect is mixed. The company has been the sole respondent only in a few cases[27]; in the majority of cases, the company and the members of its management bodies (and/or the CEO[28]) are respondents[29].

This practice has formed because of the fact that in compliance with Article 45 of the CCP, only the claimant may decide who should be the respondent in particular proceedings. Whereas Article 2.124 of the Civil Code provides that the activities of a legal person, the management bodies of the legal person or the members of its management bodies may be the object of the investigation, there is a formal ground to hold as respondents the members of management bodies together with the company.

Furthermore, as far as the application of the measures referred to in Article 2.131 of the Civil Code is concerned, it is clear that in certain instances, the CEO or (and) members of the board should also become co-respondents in the Investigation Proceedings, because there is a high probability that court judgement might affect their rights and obligations (e.g., sub-paragraph 2 of paragraph 1 of Article 2.131 of the Civil Code). In this case, the failure to join CEO or (and) members of the board as a parties to the proceedings would become an absolute ground for invalidation of the judgement in compliance with sub-paragraph 2 of paragraph 2 of Article 329 of the CCP.

If the company itself is the sole respondent in the Investigation Proceedings, following paragraph 1 of Article 47 of CCP, the members of its management bodies may join the proceedings on the side of the company as third persons without independent

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27 E.g., the ruling of the Lithuanian Court of Appeal of 10 March 2011 in civil case No. 2-278/2011.

28 Manager (sole director) of the company.

29 See the ruling of the Lithuanian Court of Appeals of 30 December 2009 in civil case No. 2A-725/2009; the ruling of the Lithuanian Court of Appeals of 30 December 2009 in civil case No. 2A-725/2009; the ruling of the Lithuanian Court of Appeals of 28 March 2008 in civil case No. 2-221/2008.

claims prior to the beginning of closing arguments[30] (See paragraph 1 of Article 47 of the Code of Civil Procedure).

3.4. The Object of Investigation

Objects of the Investigation Proceedings are provided in Article 2.124 of the Civil Code: the activity of a legal entity, the activity of the management bodies of a legal entity and the activity of the members of the management bodies of the legal entity. In its case law, the SCL reiterates the position provided in the Commentary that improper activities cover only the management of the legal entity and only the decisions of the members of the legal entity relating to the management of the legal entity.[31]

In my opinion, the object of the Investigation Proceedings is the actions of the bodies of a company in the exercise of the function of management. According to Lithuanian corporate law doctrine, the general meeting of shareholders normally does not exercise the function of management.[32] Lithuanian corporate law draws a distinction between the powers and liabilities of the board (and (or) CEO) and the general meeting of shareholders. The general meeting of shareholders and the management bodies enjoy autonomous powers and may not freely exchange them.[33]

Pursuant to paragraph 4 of Article 19 of the Law on Companies, a CEO (sole management body), but not the general meeting of shareholders, takes over the powers of the Board if the latter is not formed[34] because, the powers of the board inherently relate to the function of management[35]. Due to aforementioned regulation general shareholder meeting is not entitled to perform management function and only in extraordinary cases will be subject to investigation.

The fact that only the members of management bodies[36] and not the shareholders have statutory duties of fiduciary nature towards the company also draws a clear line between the status of board member (and CEO) and the shareholder. This diverse regulation supports the argument that shareholders are not generally supposed to manage

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30 Paragraph 1 of Article 47 of the Code of Civil Procedure: Third person without independent claims on the subject matter of the dispute may join the proceedings on the side of the claimant or the respondent prior to the beginning of closing arguments if the outcome of the case may affect their rights and obligations. They may be joined to the proceedings on a reasoned petition of the parties or on the initiative of the court.

31 The ruling of the Civil Division of the Supreme Court of Lithuania of 7 February 2005 in civil case No. 3K-3-16/2005; The Commentary of the Civil Code of the Republic of Lithuania, *supra* note 1, p. 247.

32 The Commentary of the Civil Code of the Republic of Lithuania, *supra* note 1, p. 183.

33 See Articles 2.81 and 2.82 of the Civil Code where the issue of distinction of competences is left to special laws; the Law on Companies already provides the exclusive competences of the general meeting of shareholders and the CEO which may not be delegated to other bodies of the legal person (paragraphs 4 and 5 of Article 19 of the Law on Companies).

34 Paragraph 4 of Article 19 of the Law on Companies states: "[W]here the Board is not formed in the company, the functions assigned to the scope of powers of the Board shall be fulfilled by the company manager, except where this Law provides otherwise."

35 Paragraph 2 of Article 20 of the Law on Companies states that the meeting of shareholders may take over only those functions of other bodies which are not related to the function of management.

36 Article 2.87 of the Civil Code.

the company.[37] Only directors (board members, CEO's) and not the shareholders can incur liability for the violation of statutory duties.[38]

The object of the Investigation Proceedings in case law: the assessment of the propriety of the activities of the management bodies of a legal person. i.e. whether the directors/board members of the company properly fulfil their duties as set forth by laws (as a rule, Article 2.87 of the Civil Code) and incorporation documents. The SCL practice in this respect is uniform.[39]

As a general rule, a shareholder or its conduct towards the company may not be the object of the investigation. The shareholder enjoys certain rights in the company[40], but, by his status as a shareholder, he may not impose any obligations on the company nor take decisions in the company.

In a specific case, if a shareholder holds a sufficient amount of shares to affect the decisions of the general meeting of shareholders, he may have a considerable impact on the strategic decisions of the company, but only within the limits of the competence of the general meeting. Therefore, in an aforementioned instance, the actions of the general meeting[41] rather than of a single shareholder could be the object of the investigation. But such investigation will also be limited in scope, as the general meeting of shareholders is not normally empowered to manage the company. Therefore actions of the general

37 E.g., the ruling of the Civil Division of the Supreme Court of Lithuania of 5 May 2011 in civil case No. 3K-3-228/2011: "The relationship of the head of administration of the company, as a management body of the legal person, with the legal person is specific, i.e. it is based on confidence and loyalty. The Law consolidates that a member of a management body of the legal person must act in good faith and reasonably in respect of the legal person (paragraph 1 of Article 2.87 of the Civil Code); he must be loyal to the legal person and respect confidentiality (paragraph 2 of Article 2.87 of the Civil Code); he must avoid situations where his personal interests are in conflict or may be in conflict with the interests of the legal person (paragraph 3 of Article 2.87 of the Civil Code), etc. The case law of the cassation court emphasises that the head of administration is a special subject which shall follow higher standards for his activities and liability than that applied to ordinary employees of the company; the company and the head of administration are linked by a relationship of trust (fiduciary relationship); it means that the head of administration of the company must act *ex officio* exclusively in the interest of the company; the head of the company represents the company, is responsible for the organisation of day-to-day business of the company; he must act thoughtfully, carefully, competently and in good faith and do everything in his powers to keep the company he manages operating in compliance with laws and regulations (the ruling of an expanded panel of judges of the Civil Division of the Supreme Court of Lithuania of 20 November 2009 in case *BUAB Optimalūs Finansai v. G. P.*, case No. 3K-7-444/2009; the ruling of 30 November 2009 in case *BAB Barklita v. G. B. Et al.*, case No. 3K-3-528/2009, etc.). It shall be determined whether the head of administration of the company fulfilled these duties in a particular case by using respective objective standards of conduct – the criterion applied for the conduct of a careful, cautious, prudent manager (the ruling of an expanded panel of judges of the Civil Division of the Supreme Court of Lithuania of 25 May 2006 in case *K. J. J. v. V. K. et al.*, case No. 3K-7-266/2006; the ruling of 12 June 2006 in case *AB Turto Bankas v. T. A. et al.*, case No. 3K-3-298/2006).

38 The ruling of the Civil Division of the Supreme Court of Lithuania of 5 May 2011 in civil case No. 3K-3-228/201.

39 See the ruling of the panel of judges of the Civil Division of the Supreme Court of Lithuania of 11 February 2008 in civil case *Laivų krovos AB Klaipėdos Smeltė v. UAB Birių Krovinių Terminalas, et al.*, Case No. 3K-3-73/2008.

40 See Articles 15 and 16 of the Law on Companies.

41 See The Commentary of the Civil Code of the Republic of Lithuania, *supra* note 1, p. 247.

meeting of shareholders will be the object of the investigation only to the extent these activities are related to the management of the legal entity.[42]

As far as the object of Investigation Proceedings is concerned, the position of Lithuanian courts is the same as the position of the Dutch courts, with both courts holding that only those actions which may be attributed to the company may constitute the object of the investigation; however, the Dutch Enterprise Section has decided that in specific cases actions from the general meeting of shareholders can lead to the conclusion of misconduct.[43]

To sum up, regulatory framework and the corporate law doctrine supports that only the actions of the members of the company that may be attributed to the actions of the company itself may be the object of the investigation. Consequently, the actions of a single shareholder normally do not amount to the object of the investigation.

Conclusion

Therefore, in the light of above arguments, it may be stated that the Investigation Proceedings is intended by legislature to be the legal instrument of mandatory nature and could not be effectively renounced by shareholders. The Investigation Proceedings is primarily designated to provide legal means for minority shareholders to ensure that the company is managed properly.

With reference to the Dutch model, which has been adopted by the Lithuanian Civil Code, there is no possibility to renounce the right to initiate Investigation Proceedings in the Articles of Incorporation or shareholder agreements. The mandatory nature of the Investigation Proceedings is derived from the provisions of the Code, mainly: from an active role of the court, typical to the cases with the element of public interest, from specific rules for protecting the public interest in the course of the Investigation Proceedings, also taking into account statutory duties of managers, the scope of which may not be narrowed by shareholder agreement, and the fact, that the Investigation Proceedings is generally designated to be an instrument to safeguard the interests of minority shareholders against the abuse of their rights by the company, and, finally, acknowledging the extraordinary nature of remedies available in the Investigation Proceedings.

As a general principle, the claimant's rights are more limited in the Investigation Proceedings than in a commercial dispute, respectively the court's powers are wider.

The claimant is entitled: to initiate an investigation, but it is the courts' ultimate decision whether there are sufficient grounds to commence an investigation; to define the scope of the investigation, but the court may interpret alleged limits of investigation broadly; to propose a list of experts, but the court selects experts from the list submitted

42 This argumentation does not apply when a shareholder is also a director/board member, but then his actions will be investigated as the actions of [a member of] the management body and he will be liable as a member of the management body.

43 See Timmerman, L.; Doorman, A., *supra* note 8, p. 57.

by both parties at its own discretion; to request the court to employ a specific remedy, but the court is not bound by this request.

The court, compared with a commercial dispute, plays an active role and assesses the propriety of activities of the company not from a perspective of claimant, but from much broader perspective of the company; the extent of application of the adversarial principle, as well as the principle under which the parties delimit the scope of proceedings, is much narrower in the Investigation Proceedings than in a commercial dispute. Court is empowered to employ extraordinary remedies (e.g., the liquidation of a legal entity), as compared with private commercial cases. The consequences of an application of the remedies available in Investigation Proceedings may affect the broader publics that just the parties to the dispute, as in a commercial dispute, the court normally employs remedies only to the parties.

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JURDINIO ASMENS VEIKLOS TYRIMO PRIGIMTIS PAGAL LIETUVOS RESPUBLIKOS CIVILINĮ KODEKSĄ

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Santrauka. *Šiame straipsnyje nagrinėjamas klausimas, ar 2001 CK numatytas juridinio asmens veiklos tyrimo instrumentas gali būti akcininkų valia atšauktas – įmonės steigimo dokumentuose ar akcininkų sutartyje. Autorės nuomone, atsakymas į šį klausimą yra neigiamas. Nors expressis verbis CK nepasakyta, kad teisė inicijuoti juridinio asmens veiklos tyrimą yra imperatyvi, tačiau ir normų formuluotės, nenumatančios išimčių, bei normų, skirtų viešojo intereso gynimui, gausa, pagrindžia prielaidą, kad teisė inicijuoti juridinio asmens veiklos tyrimą yra imperatyvi.*

Taip pat šią prielaidą pagrindžia ir įstatymų leidėjo tikslai – ta aplinkybė, kad JA tyrimo reguliavimą CK rengėjai perėmė iš Nyderlandų, o šio instituto imperatyvus pobūdis Nyderlandų teisėje nekelia abejonių. Nyderlandų CK normos, reglamentuojančios akcininko teisę inicijuoti juridinio asmens veiklos tyrimą (inquiry procedure) yra imperatyvios. Tiesioginis juridinio asmens veiklos tyrimo tikslas – dalyvių prašymu (tam tikrais atvejais – ir kitų suinteresuotų asmenų) išanalizuoti JA valdymo tinkamumą ir koreguoti trūkumus teismui suteiktomis priemonėmis. Lietuvos teismų praktika, nenutoldama nuo Komentaro teksto, ne kartą pakartojo, kad netinkama juridinio asmens veikla yra netinkama juridinio asmens valdymo organų ar / ir jų narių veikla. Ji suprantama kaip CK 2.86–2.87 straipsnių nuostatų pažeidimas. Šie

Kodekso straipsniai skirti reglamentuoti įstatymų numatytas valdymo organų narių pareigas juridiniam asmeniui, kurios pagal savo turinį yra fiduciarinės (lojalumo, sąžiningumo, konfidencialumo, interesų nepainiojimo), ir kurių akcininkai savo susitarimu negali nei susiaurinti, nei atsisakyti taikyti. Fiduciarines pareigas valdymo organai ir jų nariai turi ne atskiram akcininkui, o juridiniam asmeniui.

Norint nustatyti, ar valdymas tinkamas, remdamasis ekspertų išvadomis, teismas vertina, ar valdymo organai pažeidė pareigas juridiniam asmeniui. Atsakymas į šį klausimą labai priklauso nuo bendrovės sampratos. Net jei vadovausimės samprata, kad bendrovės interesai sutampa išimtinai tik su akcininkų interesais, negalėsime teigti, kad visų akcininkų – ir smulkiųjų, ir dominuojančių, interesai homogeniški ir kad įmonės interesai sutampa su dominuojančio akcininko ar jų grupės interesais, ir direktoriai tinkamai vykdo pareigas bendrovei atstovaudami dominuojančio akcininko interesams. Maža to, jei pripažinsime, kad valdymo organų tinkamas pareigų atlikimas turi atitikti visų juridinio asmens interesų grupių interesus – akcininkų, darbuotojų, kreditorių – atsakymas, kas yra tinkamas valdymas, bus dar sudėtingesnis. Vis dėlto šiuolaikinė Lietuvos teismų praktika jau gerą dešimtmetį pripažįsta, kad direktorių pareigos kyla bendrovei, kaip subjektui, turinčiam atskirus interesus nuo dominuojančio akcininko, o tam tikrais atvejais ir tretiesiems asmenims – kreditoriams. Tad tinkamu įmonės valdymu, jos tęstinumu neabejotinai suinteresuoti ne tik akcininkai, kaip tiesioginiai naudos gavėjai, bet ir kitos interesų grupės – darbuotojai, kreditoriai, tam tikra prasme egzistuoja ir viešasis interesas, kad įmonės veikla nesibaigtų dėl netinkamo valdymo. Be to,šioms interesų grupėms, o ypač smulkiesiems akcininkams, juridinio asmens veiklos tyrimas yra vienintelė tinkamo valdymo priežiūros priemonė, tuo tarpu dominuojantis akcinininkas dar gali efektyviai veikti per akcininkų susirinkimo jam suteiktas galias.

Reikšminiai žodžiai: *juridinio asmens veiklos tyrimas, įmonių teisė, smulkiųjų akcininkų apsauga, akcininkų susitarimai.*

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