GETTING THE DEAL THROUGH

Corporate Governance

Board structures and directors' duties in 42 jurisdictions worldwide

2009

Contributing editors: Ira Millstein and Holly Gregory

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Panama

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

What are the primary sources of law, regulation and practice relating to corporate governance?

Corporate governance in Panama is generally governed by, among others, Law 32 of 1927 (the Corporation Law), and the Panamanian Commercial Code of 1917. In the case of publicly traded companies, Decree Law 1 of 1998 (the Securities Law) and its regulations govern tender offers, proxy statements and rules of disclosure among other matters. In general, the following are the primary sources of law and regulations relating to corporate governance:

- Law 32 of 1927 (the Corporation Law);
- the Commercial Code of 1917;
- Decree Law No. 1 of 1999 (the Securities Law);
- Securities and Exchange Commission Agreement No12-2003, 11 November 2003 (the Agreement);
- the articles of incorporation; and
- the company by-laws, if any.

2 Responsible entities

What are the primary government agencies or other entities responsible for making such rules and enforcing them? Are there any well-known shareholder activist groups whose views are often considered?

The legislative branch is the primary entity responsible for the drafting and approval of all laws. The two main regulatory bodies that supervise the financial markets are the Superintendency of Banks (Superintendencia de Bancos) and the Securities and Exchange Commission (Comisión Nacional de Valores or CNV), which regulates public offerings and examines, supervises and controls the activities of those involved in the securities market. Through its non-binding agreement, they have issued certain guidelines and recommendations on corporate governance for all publicly traded companies. Finally, the Ministry of Economy and Finance oversees the CNV. Ultimately, of course, disputes are resolved through the judicial system or where so agreed contractually, by arbitration.

There are no well-known shareholder activist groups in Panama.

Rights and equitable treatment of shareholders

3 Shareholder powers

What powers do shareholders have to appoint or remove directors or require the board to pursue a particular course of action?

Directors of a Panamanian corporation may be appointed and removed at any time by the votes of the holders of the majority of the issued and outstanding shares with the right to vote. However, the articles of incorporation may also provide that, when a vacancy in the board occurs, the remainder of directors may appoint a replacement without the need for shareholder approval.

So long as it is not contrary to Panamanian law, the articles of incorporation may require the board of directors to seek shareholder approval before any particular action is taken. The law provides that the shareholders are the ultimate and supreme power of the corporation, which often the courts have interpreted as giving the shareholders the right to decide over just about any corporate decision without the involvement of the board of directors.

4 Shareholder decisions

What decisions must be reserved to the shareholders?

The Corporation Law grants the board of directors control over the business of the company, unless otherwise reserved for by law, the articles of incorporation, or any existing by-laws to the shareholders. Usually, fundamental corporate changes are decided at shareholders' meetings. Major corporate transactions, such as mergers and consolidations, sale of substantial company assets and dissolution require the approval of more than 50 per cent of the issued shares with the right to vote. Generally, Panamanian law requires the approval of shareholders before the following actions are taken:

- mergers and consolidations;
- amendment to the articles of incorporation;
- the sale of substantial company assets;
- the right to pledge or mortgage a company's assets to secure third party obligations; or
- the dissolution of the company.

However, the articles of incorporation may grant the directors authority to sell substantial corporate assets or pledge or mortgage them to secure third-party obligations, without the need for further shareholder approval.

5 Disproportionate voting rights

To what extent are disproportionate voting rights or limits on the exercise of voting rights allowed?

The Corporation Law allows for a corporation to issue different classes of shares, common or preferred, with different voting rights. Corporations may issue different classes of shares with similar voting rights, limited voting rights or no voting rights. The different classes of shares and the corresponding rights and restrictions must be set forth in the articles of incorporation. All shares of the same class must have, however, the same rights, preferences and restrictions, and any change to the capital structure to create new classes of shares or otherwise to adversely affect the rights and preferences of an existing class of shares must be approved by a majority of the issued and outstanding shares of each such existing class of shares with the right to vote.

6 Shareholders' meetings and voting

Are there any special requirements for shareholders to participate in general meetings of shareholders or to vote?

Unless the articles or by-laws otherwise require, it is not compulsory for companies to hold shareholders meetings annually or at other intervals. Furthermore, the Corporation Law allows for all shareholders to participate in general meetings, including those without voting rights. Shareholders may personally exercise their right to vote at a shareholders' meeting, or they may be represented through proxies, if so allowed by the articles of incorporation. Typically, where shares are registered, only those names registered in the share registry of the company are allowed to vote. In cases where shares have been issued in bearer form, shareholders are required to present their respective share certificates or other proof of ownership as may be set forth in the articles of incorporation

In the case of publicly traded companies, the Securities Law allows the CNV to regulate the solicitation and issuance of voting proxies, by requiring those who jointly solicit proxies from over 25 individual shareholders, to comply with the Securities Law or any regulation issued by the CNV in relation to the procedure of distribution of proxy and the manner in which the solicitation is to be made. Furthermore, the CNV may require that a draft proxy be submitted for review by the CNV prior to distribution to the shareholders.

7 Shareholders and the board

Are shareholders able to require meetings of shareholders to be convened, resolutions to be put to shareholders against the wishes of the board or the board to circulate statements by dissident shareholders?

Under the Corporation Law, general or special meetings of shareholders are convened by the officers of the corporation. Notice shall be given in writing to all shareholders having the right to attend and vote at said meeting by the president, vice president, secretary or assistant secretary, or by any other person authorised to do so by the articles of incorporation, including by board of directors resolution or by a given number of directors. The manner in which notice is to be given is regulated by the articles of incorporation or the by-laws. However, if the articles are silent, or the by-laws if these have been adopted, the law requires that notice be delivered personally or by mail, to each registered shareholder, no less than 10 days nor more than 60 days prior to the date of the meeting.

The holders of at least 5 per cent of the issued and outstanding shares may require a meeting to be convened by court order and to have the management of the corporate affairs reviewed by court-appointed auditors. If no evidence of mismanagement is found however, those shareholders who forced the meeting to be held and the judicially appointed auditors to review the corporate behaviour of the company, may be found liable for damages to the corporation. This right is not commonly exercised by minority shareholders and is usually considered where allegations of mismanagement have surfaced.

There is no statutory obligation for the company to circulate statements by dissident shareholders or to force resolutions to be put to shareholders against the directions of the board.

8 Controlling shareholders' duties

Do controlling shareholders owe duties to the company or to non-controlling shareholders? If so, can an enforcement action against controlling shareholders for breach of these duties be brought?

As a general principle, controlling shareholders owe no duties either to the company or to non-controlling shareholders.

9 Shareholder responsibility

Can shareholders ever be held responsible for the acts or omissions of the company?

Shareholders may not be held responsible for the acts or omissions of the company. The Corporation Law establishes that shareholders shall be personally liable to the creditors of the corporation only for an amount equal to any amount left unpaid on the par value or the subscription value (in case shares have been issued without par value) of the stock. However, no action shall be brought against the shareholder for any debt of the company, unless the corporate assets are insufficient to satisfy a judgment against it.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Panamanian corporations, whether public or private, often adopt certain tactics against takeovers. For these tactics to be valid, they must be contained in the articles of incorporation of the corporation. They may include provisions requiring supermajority voting, staggered election of directors or other measures to restrict or to force an increase of capital or transfer of issued and outstanding shares.

11 Restrictions on the transfer of fully paid shares

Are restrictions on the transfer of fully paid shares permitted, and if so what restrictions are commonly adopted?

Restrictions on the transfer of fully paid shares are permitted and often employed by corporations. As a general rule, any restriction on transferability of shares has to be clearly stated in the articles of incorporation. Pre-emptive rights and rights of first refusal are the most commonly adopted restrictions. The Corporation Law however, prohibits an absolute restriction on the transferability of shares.

12 Compulsory repurchase rules

Are compulsory share repurchase rules allowed? Can they be made mandatory in certain circumstances?

Compulsory and mandatory repurchase of shares is allowed as long as such rules are clearly stated in the articles of incorporation. The Corporation Law is not specific as to when and under what circumstances a company may repurchase its shares. However, a company may not purchase or otherwise redeem its issued stock if, after such redemption, the corporate assets are less than the liabilities plus the remaining stated capital. Furthermore, no corporation may directly or indirectly vote any shares of its own stock kept in treasury.

Responsibilities of the board (supervisory)

13 Board structure

Is the predominant board structure for listed companies best categorised as one-tier or two-tier?

Companies are required to have a single board of directors who generally have control over the management of the affairs of the company. It is best categorised as one-tier board structure.

14 Board's legal responsibilities

What are the board's primary legal responsibilities?

The general duties of directors include the sound management of the business of the company and conduct of its accounting, and compliance with the laws, the articles of incorporation, the by-laws (if any), and resolutions of the shareholders. The board of directors may exercise all of the powers of the corporation, except such powers that are by law, the articles of incorporation or the by-laws, reserved to the shareholders.

15 Board obligees

Whom does the board represent and to whom does it owe legal duties?

The board of directors manages the day-to-day business of the corporation and in doing so, it represents the best interests of the corporation and its shareholders. Directors are generally considered to have received a mandate to manage the affairs and assets of the corporation. As such, directors are responsible for discharging their mandate with due care, and may become personally liable not only for fraud and wilful misconduct but also for negligence in the discharge of their duties.

16 Enforcement action against directors

Can an enforcement action against directors be brought on behalf of those to whom duties are owed?

Although generally speaking, directors are not personally liable for the obligations of the corporation, they may become jointly and severally liable if they are found not to have discharged their duties as directors with the degree of care that ordinarily prudent men would exercise in the discharge of their own affairs. Directors are in a principal/agent relationship with the corporation they serve. Directors who have voted against a resolution of the board of directors which gave rise to personal liability, as well as directors who were not present with reasonable cause at the meeting where such resolution was adopted, are not personally liable for actions or resolutions adopted by the board at said meeting. If directors are found liable for violation of the general duty of care or any other provision imposed by law, they would be held jointly and severally liable for damages arising from their breach of the duty of care. A claim may be filed by the company itself or, derivatively, by a shareholder. Generally speaking a director of a Panama corporation may not be held personally liable either to the company, its shareholders or any other person, unless a resolution authorising such action against the director is adopted by the shareholders of the company. However, in case of fraud in, for instance, declaring a dividend or authorising a capital reduction from insufficient funds, the directors who assent to such action would be personally and jointly and severally liable to the creditors of the company, with or without shareholders' authorisation of the claim. Also, certain other causes of action such as liabilities arising for violation of the directors' duties as trustees in liquidation for example are not dependent on shareholders' authorisation. Finally, in the case of financial, banking or securities entities, certain criminal sanctions may apply to directors if involved in authorising or approving improper disclosures, refusing to cooperate with an inspecting authority or, in case of banks, when such banks exceed statutory lending limits.

17 Care and prudence

Do the board's duties include a care or prudence element?

The standard of care to which directors are generally subject is that which 'ordinarily prudent men would usually exercise in the discharge of their own affairs' (see question 16).

Directors of public companies may also become personally liable for breach of a duty of loyalty and for violation of certain restrictions on self-dealing.

18 Board member duties

To what extent do the duties of individual members of the board differ?

All members of the board of directors are subject to the same standard of care, ie that which 'ordinarily prudent men would usually exercise in the discharge of their own affairs'. Thus, generally speaking, all directors owe the same duty of care as would ordinary, careful and prudent men in the conduct of their own personal affairs, to the company and the shareholders, regardless of their different, individual skills and experience.

19 Delegation of board responsibilities

To what extent can the board delegate responsibilities to management, a board committee or board members, or other persons?

Generally speaking, and except as expressly reserved for the shareholders in the law, the articles of incorporation or the by-laws, the business of a corporation is directly managed by the board of directors.

Additionally, the board of directors has the power to appoint two or more of its members to constitute one or more committees with all the powers of the board, subject to any restrictions that may be contained in the articles, by-laws or resolution appointing the committee or committees. The board may also grant general or limited powers of attorney to other individuals, who need not be directors or corporate officers.

20 Non-executive and independent directors

Is there a minimum number of 'non-executive' or 'independent' directors required by law, regulation or listing requirement? If so, what is the definition of 'non-executive' and 'independent directors' and how do their responsibilities differ from executive directors?

The question of the role of non-executive directors does not arise under Panama law. Directors can be executive or non-executive, as preferred in each individual case, and their legal treatment as directors is the same. Furthermore, there is no general requirement that directors be independent of the company. However, there are specific cases of certain regulated companies where a percentage of directors are required to be independent of the company. For instance, in an investment company within the meaning of the Securities Law, no less than 20 per cent of the board of directors must be independent of the company or 'outside' directors. Finally, the duties and liabilities of non-executive directors are generally the same as for all other directors (see 16 and 17 above).

21 Board chairman and CEO

Do law, regulation, listing rules or practice require separation of the functions of board chairman and CEO? If flexibility on board leadership is allowed what is generally recognised as best practice and what is the common practice?

There are generally no restrictions on the roles of individual board members. Therefore, a director can also act as chairman and CEO. There is no best practice standard concerning separation or joining of these functions in Panama and both figures are found in practice in the structure of Panamanian companies.

22 Board committees

What board committees are mandatory? What board committees are allowed? Are there mandatory requirements for committee composition?

Except for the case of certain regulated financial institutions (banks for example), there are no mandatory requirements for the existence of given board committees or for committee composition (see question 19).

23 Board meetings

Is a minimum or set number of board meetings per year required by law, regulation or listing requirement?

There is no minimum or set number of board meetings imposed by law, regulation or listing requirements.

24 Board practices

Is disclosure of board practices required by law, regulation or listing requirement?

There are no legal requirements of disclosure of board practices. Additionally, there are no legal requirements that bind directors to disclose specific information about the company if requested by individual shareholders. However, where a duly adopted resolution of shareholders requires the disclosure of certain information, the directors are under an obligation to disclose it.

Listed companies or companies regulated by the securities and banking laws are required to disclose certain specific information when requested or demanded by the applicable regulatory agency. Generally speaking, regulatory agencies require listed companies to file quarterly and annual reports of the company's financial and operating results, audited end-of-year or unaudited financial statements for the respective period, and to disclose certain material events identified in the Securities Law, which may affect the value of registered shares or other securities.

25 Remuneration of directors

Is there any law, regulation, listing requirement or practice that affects the remuneration of directors, the length of directors' service contracts, loans to directors or other transactions between the company and any director?

No, there are no laws or regulations imposing standards or limits on directors' remuneration, length of directors service (generally not imposed by contract) or any other transactions between a director and the company, except that in the case of a conflicted director of a public company, he or she can participate at the meeting where the transaction is being approved and may be counted for quorum purposes, and even vote at such meeting. However, the board's decision must be informed to the general shareholders' meeting, presumably so that it may approve or disapprove the corporation's commitment.

26 Remuneration of senior management

How is the remuneration of the most senior management determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of senior managers, loans to senior managers or other transactions between the company and senior managers?

Remuneration of senior management is usually set by resolution of the board of directors. There is no law, regulation, listing requirement or practice that affects or limits remuneration to senior management. Except for the case of regulated financial institutions, insurance companies, and broker-dealers, there are no limits to loans or other transactions between the company and senior management.

27 D&O liability insurance

Is directors' and officers' liability insurance permitted or common practice? Can the company pay the premiums?

Panama companies may purchase D&O insurance to protect their directors, but such insurance would not be enforceable with respect to liabilities resulting from fraud, wilful misconduct or gross negligence. There are no legal provisions which would prevent the company from paying the insurance premium.

28 Indemnification of directors

Are there any constraints on the company indemnifying directors in respect of liabilities incurred in their professional capacity? If not, are such indemnities common?

A Panama company may lawfully indemnify its directors for all liabilities that they may incur in the discharge of their duties as directors, unless such liabilities result from fraud, wilful misconduct or gross negligence. Any indemnity against fraud, wilful misconduct or gross negligence would be contrary to public policy and not enforceable.

29 Employees

What role do employees play in corporate governance?

Generally speaking, employees do not play any role in corporate governance.

Disclosure and transparency

30 Corporate charter and by-laws

Are the corporate charter and by-laws of companies publicly available? If so, where?

Panamanian Law requires that all companies register their articles of incorporation at the Panamanian Public Registry. By-laws are not required to be adopted or registered.

31 Company information

What information must companies publicly disclose? How often must disclosure be made?

All companies must make public information contained in the articles of incorporation, which is registered at the Panamanian Public Registry. By law, the articles of incorporation must include, and thus public information will contain, among other things, the name of the corporation, the objects of the corporation, the authorised capital in its different classes, and the different rights, preferences and restrictions pertaining to each class of shares, restrictions on the issuance or the transferability of shares, rights of redemption, the company's domicile, the identity and method of election of directors and officers, among other information.

Update and trends

There are no pending significant proposals for new legislation or regulation regarding corporate governance. In 2009, a new Criminal Code was enacted containing certain financial crimes that may involve corporate directors (see question 16).

We do not at this time anticipate that the current financial crisis will lead to new corporate governance regulations in Panama.

As for publicly traded companies, they must file quarterly and annual reports, audited financial statements, reports of material events that may affect the value of their registered shares or other securities, as described in the Securities Law, among others.

Hot topics

32 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration?

Generally, shareholders do not have an advisory role or other vote regarding executive remuneration.

33 Proxy solicitation

Do shareholders have the ability to nominate directors without incurring the expense of proxy solicitation?

Yes. Shareholders may act directly at meetings to exercise their rights to nominate directors without involving a proxy.

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