LAW ON COMPANIES

1.00

WHITE BOOK BALANCE SCORE CARD

Recommendations:	Introduced in the WB:	Significant progress	Certain progress	No progress
Limited liability partnerships (LLPs) should be prescribed by the Law.	2013			√
The new confusing provisions in relation to the (i) agreement between the company and a new shareholder regarding the share transfer, and (ii) nullity of share transfer agreement should be amended to avoid legal uncertainty.	2022			√
The provisions in the Law on Contracts and Torts that deal with limitations to the authority of a company's representatives should be harmonized with the provisions of the Law	2011			√
Consequences for breaching the share transfer restrictions provided under the Memorandum of Association should be prescribed by the Law.	2022			√
Consequences for adopting the decisions by various corporate bodies (such as board of directors) contrary to the law should be prescribed by the Law.	2022			√
Common practical issues should be resolved, such as regulating shareholders' additional payments, e-signing, representatives liabilities, share capital increase and approving the transactions involving the personal interest.	2018			√
Difference between regular and interim dividend should be prescribed in a less formalistic approach.	2022			√
Corrections of technical flaws in the Law should be made to eliminate inconsistencies and provide clear procedures and competencies, harmonizing provisions within the Law itself.	2013			√

CURRENT SITUATION

The Companies Law ("Official Gazette of the Republic of Serbia", Nos 36/2011, 99/2011, 83/2014, 5/2015, 44/2018, 95/2018, 91/2019 and 109/2021) ("Law") came into force on 4 June 2011 and is applicable as of 1 February 2012.

By signing the Stabilization and Association Agreement with the European Union, the Republic of Serbia undertook the obligation to harmonize its domestic law with the EU acquis. Within the negotiations on the accession of the Republic of Serbia to the EU, Chapter 6 – Law has a special role, which includes issues of establishment and operation of companies in EU member states, in accordance with which the Republic of Serbia would be provided with better business conditions on the EU market, simplified procedures and the possibility of establishing new forms of economic entities. The Law is an indicator of progress in harmonizing the legislation of the Republic of Serbia with the EU acquis, which is important for the process of integration of the Republic of Serbia into the EU.

The main characteristics of the Law are:

- application of standards harmonized with EU legislation;
- harmonization with the Law on the Capital Market;
- certain problems that were a characteristic of the previous regulation have been resolved;
- the distinction between (public) joint-stock companies and other forms of business organization and;
- single-tier and two-tier management systems.

The latest amendments to the Law were in November 2021 which is the seventh time the Law undergoes changes since it was enacted thirteen years ago. These latest amendments introduced various changes, such as:

- Each company must register for use of e-government services.

- The companies may have only legal entities as directors.
- Provisions on approving the transactions involving personal interests contain more details and duties.
- There are new (confusing) provisions in relation to the (i) agreement between the company and a new shareholder regarding the share transfer, and (ii) nullity of share transfer agreement (as explained below in more detail).
- More information must be registered in relation to the company's seat.
- For all individuals registered in the companies' registry (director, shareholder, member of the supervisory board, etc.) gender is mandatory as registration data.
- Each joint stock company must provide to a shareholder, who initiated litigation procedure against the company based on legal grounds provided by the Law, the information related to the court case (even if in ordinary course of dealings such information would not be available to such shareholder).
- The total remuneration of the director (of a joint stock company) includes salary or other remuneration provided in employment/management agreement and may include the right to incentives through the allocation of shares of the company or another affiliate of the company. Also, the shareholders holding at least 5% of the share capital are now entitled to access the documents and data on the amount and structure of the total remuneration for each director and member of supervisory board.

The public joint stock companies are now obliged to prepare the policy which will in detail regulate the fixed and variable parts of compensations to directors and supervisory board members. Such policy is to be adopted by the shareholders meeting, and any payments must be made in accordance with that policy. Additionally, the detailed report on the compensations to directors and supervisory board members must be part of the annual financial statements of the company, is subject to audit and must be publicly available for at least 10 years.

POSITIVE DEVELOPMENTS

There are no improvements in terms of fulfilment of the recommendations published in last year's White Book.

REMAINING ISSUES

As previously stated, one of the disadvantages of the Law continues to be the absence of the concept of limited liability partners in a partnership. The existence of such a concept would be particularly relevant for partners in professional partnerships, since they should be allowed to enjoy limited liability protection, while third parties' risks could and should be covered by liability insurance.

The latest amendments of the Law we reflected on earlier introduced a rather confusing provision requiring that for a third party to become a shareholder in a LLC, an agreement between that party and the company itself must be made (person nominated by the shareholders meeting signs on behalf of the company). It seems that the purpose of this amendment is to provide a legal basis for the existing practice where in case of a share capital increase by a third party, the Serbian Business Registries Agency ("BRA") required an agreement on accession to be signed between existing and new shareholders. According to the BRA, this provision will apply only in special (in practice very rare) cases where the company's memorandum of association provides that consent of the company itself is required for transfer of the share to a third party and in case of share capital increase, as stated. There is a concern that the wording of the provision is such that this provision apparently applies even if a third party becomes a shareholder by acquiring shares from the existing shareholder. Requiring such an agreement does not only lack purpose but is arguably detrimental to the status of minority shareholders in LLC's. It appears that this provision may give the right to majority shareholders to block the minority shareholders to rightfully transfer their shares to third parties (by blocking execution of such an agreement at the level of shareholders' meeting). It seems that this was not the intention of the legislator but is apparently an unfortunate inadvertent effect.

The latest amendments also contain a provision that, if a nullity of a share transfer agreement is established by a court ruling, the parties can request from the BRA to change the registration of the title to the affected share. It is not clear whether this newly introduced article will override the principle of reliance in the registered data, providing that the parties cannot bear negative consequences if they relied on the registered data (which is of paramount importance for the certainty of legal transactions), and whether subsequent acquirers of the share (in case of sale chain) act-

ing in good faith would bear consequences to their title to the share if the title of one of the previous sellers in the sale chain would be declared null. We hope this controversy will be resolved in court practice in favour of the reliance principle, but until then the huge legal uncertainty remains.

On a related note, the Law allows various restrictions (regarding the share transfer) to be prescribed in the company's memorandum of association. However, there is no prescribed consequence if such restrictions are breached, which may limit practical aspects of limitations provided under the memorandum of association.

The latest amendments also enhanced "mechanism" in relation to the approval of transactions involving personal interests. In general, it seems that duty to publish such transactions (that is, to publish the intention of entering into such transactions) for companies that are not public joint-stock companies is excessive and contrary to the nature of "private" companies. Parallel to this general notion that these duties may be deemed as too burdensome, in any case it should be: (i) clarified that there is no need for publishing the details about the related party transaction, if there an exception to a duty to approve respective personal interest transaction, (ii) clarified if an exception related to the Republic of Serbia refers to the transactions only involving the Republic of Serbia or transactions with companies where the Republic of Serbia is shareholder (irrespective if Republic of Serbia is a party to the respective transaction); (iii) provided that subsequent approval for these transactions is allowed.

The "standard" comment about e-signing under Serbian legislation should be considered from the perspective of executing the decisions of corporate bodies as well – electronic signatures recognized in other countries should be acceptable in Serbia (and not only qualified electronic certificates in Serbia). This would significantly speed up the business operations.

In relation to the representatives' responsibilities, it is required to (i) harmonize non-compete duty with employment regulation and competition protection rukles, (ii) reflect provisions regarding director's liability in joint stock companies (Article 415) to the LLCs as well, (iii) clarify if fiduciary duties are applicable to the representatives of the branch and representative offices. Also, the Law should prescribe consequences if decisions of various management boards (e.g. board of directors) are not adopted in line with the law.

The provisions of the Law restricting the powers of representatives to represent the company are inconsistent with the relevant provisions of the Law on Contracts and Torts. It should be clear that the respective provisions of the Law, as lex specialis, have a prevailing effect.

Currently, any dividend paid between the regular shareholders meetings are deemed as interim dividend (which triggers additional duties for the companies). There is no reason that distribution of dividends (representing the profit based on annual financial statements) made after the regular shareholders meeting is considered as an interim dividend i.e. current approach is too formalistic.

Other inconsistencies of the Law include the provision prohibiting a single-member LLC from acquiring own shares, which is contrary to the Law's provisions on status changes.

It is also required to clarify if the evaluation made by external expert is always needed when the share capital is increased by the in-kind contribution.

FIC RECOMMENDATIONS

- Limited liability partnerships (LLPs) should be prescribed by the Law.
- The confusing provisions in relation to the (i) agreement between the company and a new shareholder regarding the share transfer, and (ii) nullity of share transfer agreement should be amended to avoid legal uncertainty.
- The provisions in the Law on Contracts and Torts that deal with limitations to the authority of a company's representatives should be harmonized with the provisions of the Law.

- Consequences for breaching the share transfer restrictions provided under the Memorandum of Association should be prescribed by the Law.
- Consequences for adopting the decisions by various corporate bodies (such as board of directors) contrary to the law should be prescribed by the Law.
- Common practical issues should be resolved, such as e-signing, representatives liabilities, share capital increase and approving the transactions involving the personal interest.
- Difference between regular and interim dividend should be prescribed in a less formalistic approach.
- Corrections of technical flaws in the Law should be made to eliminate inconsistencies and provide clear procedures and competencies, harmonizing provisions within the Law itself.