Minimization of Costs for Redemption of Shares at Request of Shareholders

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**ABSTRACT**

This paper analyzes the options of minimization of the company costs associated with the redemption of shares at the request of shareholders in accordance with the Article 75-76 of the Federal Law Russian Federation "On Joint Stock Companies".

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1. Introduction

The special shareholders’ interest protection mechanism based on recovery of their investments by the company applies in the Corporate Practices. When resolution on running of critical corporate events, which may significantly change conditions of participation in the company, is passed by General Shareholder Meeting, the shareholders who did not uphold this resolution (voted against or did not participate in the vote) are entitled to demand the redemption of shares held by them.

Usually, these critical corporate events include resolution on reorganization of the company and approval of major transactions with company assets. These events may change the company’s economic structure due to asset outflow, substitution thereof with less liquid ones and increment of liabilities. Such events include alternation of the company Articles that leads to reduction of scope of shareholder rights, and, regarding public joint stock companies, resolution on delisting of equity securities and/or resolution on alteration of the company Articles that leads to elimination of evidence that the company is public (p.1 Art. 75 the Federal Law "On Joint Stock Companies").

In virtue of criticality of such issues, the larger quantity of votes of the General Shareholder Meeting participants is required to pass the resolution thereon. Such resolutions are passed by three-fourths majority of votes of the voting shares owners who participate in the General Shareholder Meeting (p.4 Art. 49 of the Federal Law "On Joint Stock Companies"). Resolution on alternation of the company Articles that leads to elimination of evidence that the company is public is passed by the General Shareholder Meeting by majority of 95 percent of votes of all shareholders who own the company shares of any class (type) (p. 4 Art. 7.2 of the Federal Law "On Joint Stock Companies").

If large majority of the shareholders participating in the Meeting supports the running of the corporative events stated above, the minority that does not uphold the resolution on running thereof is entitled to demand redemption of shares held by them from the company. Investments are recovered at the price of not lower than current market value of securities held by them. The principle “money instead of shares” applies.

The shareholders who did not take part in the vote or voted against the issue put to a vote are entitled to demand the redemption of shares held by them within 45 days from the date of Meeting.
This method of economic interest protection is not associated with any violation of their rights by the company. The company passes totally legal resolution but some shareholders may find impact thereof as negative. Here the question is not about violation of shareholder rights but about the special protection mechanism of economic (investment) interests of separate shareholder groups in case of passing by the company resolutions which can significantly change conditions of participation therein.

However this mechanism has certain negative impact. Redemption of allotted shares by the company aggravates the economic situation therein. The outflow of the most liquid assets – money occurs. In exchange the company receives property with doubtful economic properties which is not recognized as asset as it does not take part in business activities and does not provide economic benefits. This property is economically barren. Redemption of allotted shares by the company reduces the assets and company equity capital.

- **Assets** — Resources controlled by the company as a result of events of the previous periods from which the company expects to get economic benefit in the future.

- **Property** — Legal conception used to classify objects of civil rights in order to institute specific distribution rules for each of them. The property includes the following:
  - Items of property including cash money and certified securities;
  - Noncash funds, uncertified securities;
  - Property rights.

Along with property the Russian Civil Code specifies the following objects of civil rights:

- Protected intellectual property and equated means of individualization (intellectual property);
- Intangible asset.

Not all property possessed by the corporation is its asset, but only property that is expected by the company to be economically beneficial. If the property is an object of legal relationship (subject of transaction), but is not expected to be economically beneficial, in such case the property is not recognized as asset\(^1\).

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\(^1\) Relation between assets and property conceptions is duly illustrated by the following example. The picture placed at the Director’s receiving room was presented as a gift for corporation anniversary. This is property with which the transactions can be made, for example the picture can be presented for anniversary of another
Acquisition by the company of shares is company costs i.e. share outflow that leads to reduction of the company capital.

- **Costs** – outflow of economic benefits during the accounting period occurred as outflow or reduction of assets or liability increment which leads to the capital reduction not associated with distribution to the company shareholders.

- **Expenses** – company resources used for manufacturing and sales of products during the certain period. Execution of expenses – operations resulting in transformation of assets of one form into those of another. In contrast to costs, expenses do not result in assets outflow but only change their composition.

On one hand, redemption by the company of shares at shareholder’s request is the protection mechanism of their interests. On the other hand, this mechanism has negative impact on the company, such as outflow of the liquid assets. Conflict of interests of the company and its shareholders occurs. Naturally, the company endeavors to limit negative economic impact of redemption of shares from the shareholders. The Corporate Law responds to this conflict of interests in a certain manner. In order to protect interests of the company and the rest of shareholders the maximum sum of costs associated with redemption of shares was limited. Costs cannot exceed 10% of the company net assets available at the date of resolution on running of corporative events stated above.

For the purpose of protection of shareholders’ interests the special procedure for determination of share repurchase price is established. In that case the threshold price principle popular in the Corporate Practices applies. This principle means legal assignation of the threshold which shall not be exceeded by the share price for running of the certain corporate event. Shares are redeemed by the company at the price set by the company Board of Directors which shall not be lower than market value determined by assessor without considering its change as a result of company’s actions that lead to creation of right to demand assessment and redemption of shares (p.3 Art.75 of the Federal Law "On Joint Stock Companies"). Share repurchase price is determined by the company Board of Directors in advance and is notified to shareholders at least 20 days before the date of Meeting.

The company and shareholders that are aware of the sum of net assets and repurchase price for single share determine the maximum quantity of shares that can be redeemed by the corporate. However, this picture is not used in business activity in order to get the economic benefits and thus is not recognized as asset.
company. If quantity of shares presented for redemption exceeds this value, the shares are redeemed in proportion to shareholder’s share fraction in total quantity of shares presented for redemption.

Dominating shareholders endeavor to ensure passing of resolution that they are interested in by the General Shareholder Meeting as well as to reduce outflow of the company assets in favor of dissenting minority. For that purpose the following scheme is applied in the Corporate Practices. Majority shareholder voted “for” respective resolution having ensured its adoption during the Meeting. His friendly partner voted at least one share “against” or did not take part in the Meeting (vote). After the Meeting majority shareholder transferred a part of his shares to the partner. This shareholder presented for redemption the block of shares that had been formed after the Meeting. Risen demand exceeds quantity of shares that can be redeemed by the company. In that case shares are redeemed from the shareholder in proportion to his share fraction in total quantity of shares presented for redemption. The more shares are presented for redemption by majority shareholder’s partners the fewer shares are redeemed from minority shareholders. The sum payable to other shareholders due to redemption of shares from the majority shareholder’s partner is reduced. The assets outflow is reduced in favor to minority shareholders by redistribution of the part of this outflow in favor to majority shareholder’s partner.

In order to prevent such negative actions the supplement to the Corporate Law according to which the maximum quantity of shares, redemption of which may be demanded by the shareholder, shall not exceed the quantity of owned shares of the respective class (type) determined on the basis of listed persons entitled to participate in General Shareholder Meeting is introduced\(^2\).

When this amendment is introduced the shareholder cannot present for redemption the shares which he received after the Meeting\(^3\).

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\(^2\) Introduced by the Federal Law N 210-ФЗ dated 29.06.2015.

\(^3\) This deprives the shareholders of the protection of their economic interests in relation to legally acquired securities. After the Meeting shareholder received supplementary shares as a result of the legal succession (came into inheritance or reorganization was completed), the court decision on restoration of rights for shares came into effect, the court applied consequences of invalidity of transaction on securities alienation (restitution), securities are received as indemnity, performance time of a repurchase agreement came etc. The shareholder is not entitled to demand redemption of these securities, notwithstanding negative impact of resolution adopted by General Shareholder Meeting.
2. Analysis of Efficiency of Protection of Minority Shareholders

Let us analyze how this supplement to the Corporate Law protects against possible abuses.

For example, the shares of the single class – common are allotted in the company. Dominating shareholder initiates the resolution on reorganization of the company. Meanwhile, he endeavors to reduce quantity of shares that may be redeemed from minority shareholders who do not uphold the resolution. Prior to list the persons, who are entitled to participate in the Meeting, the majority shareholder transfers the part of his shares to the partners who either do not participate in the Meeting (vote) or participate but vote against the issue put to a vote. This allows the shareholders to present their shares for redemption as they received them before the persons who are entitled to participate in the Meeting were listed. Quantity of shares presented for redemption exceeds the maximum quantity of shares that may be redeemed in case of established net assets and repurchase price. In that case, shares are redeemed from the shareholders in proportion to share fraction of every shareholder in total quantity of shares presented for redemption.

When analyzing the situation, minority shareholders’ behaviors adverse for the majority shareholder are considered.

The first adverse condition is that all opponents of the issue put to a vote do not participate in the Meeting and majority shareholder with his partner shall provide the quorum in respect of this issue by means of their shares.

The second adverse condition is that all opponents of the issue put to a vote participate in the Meeting and vote against it. The majority shareholder shall provide adoption of resolution on this issue by means of his shares.

It is necessary to determine the minimum quantity of shares that shall be kept by the majority shareholder in order to respond adequately to any negative circumstances.

The task is complicated by the fact that majority shareholder shall ensure fulfillment of the following conditions when transferring the part of his shares to the partner before the date of listing of the persons entitled to participate in the Meeting:

- The maximum possible quantity of shares which will be presented for redemption shall be transferred;
• Meanwhile, the quantity of shares sufficient to ensure the quorum in respect of the issue put to a vote shall be kept in case if all opponents of this issue do not participate in the Meeting;

• During the Meeting the quantity of votes sufficient to pass the resolution on the issue put to a vote shall be ensured in case if all opponents of this issues participate in the Meeting and vote “against”.

Enter designations

\[ N \] – quantity of the company shares held by the persons entitled to participate in the General Shareholder Meeting.

\[ V \] – Quantity of shares owned by the dominating shareholder (group of affiliated persons), who are interested in adoption of resolution on the issue put to a vote.

\[ Z \] – Quantity of shares owned by the majority shareholders who do not uphold the considered resolution (all actual opponents of the issue put to a vote).

The majority shareholder shall proceed from the most negative scenario when all opponents of the resolution concerned participate in the Meeting and vote “against”.

Prior to list the persons entitled to participate in the General Shareholder Meeting, the majority shareholder divided in advance the owned shares into the following parts.

\[ V_1 \] – Shares transferred by the majority shareholder to his partner who does not participate in the Meeting and demands the redemption of shares held by him. These shares are not taken into account in the quorum.

\[ V_2 \] – Shares transferred by the majority shareholder to another partner who participates in the Meeting, votes against the resolution concerned and demands the redemption of shares held by him. These shares are taken into account in the quorum.

\[ V_3 \] – Shares kept by the majority shareholder which he votes for the issue put to a vote. These shares are taken into account in the quorum.

\[ Q \] – The quorum in respect of the issue put to a vote:

\[ Q = \frac{1}{2} N + 1. \]

Introduced values satisfy the following identities:

\[ N = V + Z \]

\[ V = V_1 + V_2 + V_3 \]
$V_1; V_2; V_3$ – Values by means of which the majority shareholder can influence the quantity of shares redeemed from minority shareholders who do not uphold the resolution on issue put to a vote.

These controlled variables subject to constriction that consist in observance of certain inequalities.

- The first constraint is related to provision of quorum – it is required that the majority shareholder and his partner have the quantity of votes sufficient to provide quorum in respect of issue put to a vote in case if all opponents of this issue do not participate in the Meeting.

$$V_1 \geq Q \text{ or } V_2 + V_3 \geq Q$$

- The second constraint is related to assurance of adoption of resolution on the issue – it is required that the majority shareholder has quantity of votes sufficient to ensure adoption of resolution on the issue put to a vote in case if all opponents of this issue participate in the Meeting and vote “against”.

As a matter of principle, in order that General Shareholder Meeting passes the positive resolution on the issue put to a vote, at least $\frac{3}{4}$ of meeting participants’ votes shall be casted for this resolution. It is required that quantity of shares held by the Meeting participants (group of participants) upholding this resolution exceeds the quantity of shares held by the Meeting participants who do not uphold respective resolution threefold.

$$V_3 \geq 3(V_2 + Z) \text{ or } V_3 - 3V_2 \geq 3Z$$

$$3Z = C$$

- The third constraint – it is required that the majority shareholder transfers to his partners the maximum possible quantity of shares which they present for the redemption in order to reduce minority shareholder's fraction in the total quantity of shares presented for redemption.

Remember that sum of costs for redemption of shares shall not exceed 10% of the company net assets. This constraint determines the maximum quantity of shares that can be redeemed by the company at the certain repurchase price.

$P$ – Repurchase price for single share.

$NA$ – Company net assets.
A – Maximum quantity of shares that can be redeemed in case of availability of net assets and repurchasing price.

\[ A = 10\% \frac{NA}{P} \]

The majority shareholder manipulating the values \( V_1 \); \( V_2 \) and \( V_3 \) may provide the situation when quantity of shares presented for redemption exceeds the maximum quantity of shares that may be redeemed in case of established net assets and respective repurchasing price. This results in redemption of not all shares from the minority shareholders who demanded it. Meanwhile the more shares are presented for redemption by the majority shareholder’s partners the fewer shares are redeemed from the minority shareholders.

Majority shareholder endeavors to increase the values \( V_1 \) and \( V_2 \), in order that quantity of shares presented for redemption exceeds the quantity of shares that can be redeemed by the company to the maximum extent.

\[ V_1 + V_2 + Z > A \text{ or } V - V_3 > A - Z \text{ hence } V_3 < V + Z - A \]

\[ V + Z - A = B \text{ or } N - A = B \]

B – Quantity of non-redeemable shares.

\( V_3 \leq B \) – quantity of shares kept by the majority shareholder to vote “for” (redemption of which he cannot demand) that shall not exceed number of non-redeemable shares.

Limitation system was developed in relation to variables \( V_2 \) and \( V_3 \) controlled by the majority shareholders.

\[
\begin{align*}
V_2 + V_3 & \geq Q \\
V_3 - 3V_2 & \geq C \\
V_3 & \leq B
\end{align*}
\]

(1)

Remember the natural constraints:

\( V_2 \geq 0 \) and \( V_3 > 0 \)

Present the coordinate system for \( V_2 \) and \( V_3 \) on the plane.

Represent a set of solutions of each of three above the formulated inequalities (1) formulated above. The lines described by the following equations are boundaries between these solutions:

\[ V_2 + V_3 = Q \]
\( V_3 - 3V_2 = C \)

\( V_3 = B \)

Denote these lines as “Q”, “C” and “B” accordingly.

The line “Q” defines the possible combinations of \( V_2 \) and \( V_3 \), the sum of which provides the quorum of the General Shareholder Meeting without participation of minority shareholders (Fig.1).

The line “C” defines all possible combinations of \( V_2 \) and \( V_3 \), at which the majority shareholder can ensure adoption of resolution on the issue put to a vote in case if all minority shareholders participate in the Meeting and vote against this issue (the most negative variant) (Fig. 2).
Conjunct multiple combinations of $V_2$ and $V_3$ constrained by the line “Q” and multiple combinations thereof constrained by the line “C”. This conjunction enables to detect possible combinations of $V_2$ and $V_3$ which simultaneously allow the majority shareholder to provide the quorum of the General Shareholder Meeting and adopt the resolution on the issue put to a vote.

This conjunction has two modifications depending on $C \leq Q$ or $C \geq Q$.

The situation when $C \leq Q$ is presented in Figure 3. Intersection of the lines “Q” and “C” defines the combination of $V_2$ and $V_3$, at which the minimum value of the indicator $V_3$ is achieved. This is the minimum quantity of shares that may be kept by the majority shareholder and voted by him “for” adoption of issue. This minimum quantity of shares kept by the majority shareholder corresponds to the maximum sum of $V_1$ and $V_2$ which is the maximum quantity of shares that can be transferred by the majority shareholder to his “partners” in order to present them consequently for redemption.

Denote the intersection point of the lines “Q” and “C” by the symbol “O” and describe its coordinates:

$V_2 = (Q - C)/4$

$V_3 = (3Q + C)/4$

The situation when $C \geq Q$ is shown in Figure 4.
In such case the minimum value of the indicator $V_3$ is achieved at the point “C” having the following coordinates:

$V_2=0$

$V_3=C$ or $V_3=3Z$

In such case the majority shareholder cannot transfer the part of his shares to the partner who has participated in the Meeting and voted against the issue put to a vote ($V_2=0$). The majority shareholder may transfer the part of his shares only to the partner who does not participate in the Meeting ($V_1$).

The horizontal line “B” is added to the lines “Q” and “C” in Figure 5. This line defines multiple possible combinations of $V_2$ and $V_3$, at which the majority shareholder provides the conditions in order to ensure that the minimum quantity of shares is redeemed from the minority shareholders.
Conjunction of multiple combinations of $V_2$ and $V_3$ constrained by the lines “Q” and “C” with multiple of combinations thereof are constrained by the line “B” provides the following variants.

If the point “O” exists (intersection point of “Q” and “C”) the line “B” shall be drawn not lower than this point.

In order to ensure the availability of the point “O” it is necessary that $Q \geq C$.

This inequality may be rearranged into the following inequality:

$$Z \leq \frac{1}{6}N + \frac{1}{3}$$

It is possible to neglect the share fractional portion as it does not affect the result that allows to express the inequality in percentage:

$$Z \leq \frac{1}{6}N \text{ or } Z\% \leq 16,7\%.$$  

In order that the horizontal line “B” passes not lower than the point “O” the following condition is required:

$$B \geq \frac{3Q+C}{4}.$$  

This inequality can be rearranged into the following: $Z \leq \frac{5}{6}N - \frac{4}{3}A - \frac{1}{2}$.  

It is possible to neglect the share fractional portion as it does not affect the result that allows to express the inequality in percentage:

$$Z\% \leq 83,3\% - \frac{4}{3}A\%.$$
Multiple combinations of $V_2$ and $V_3$ at which the point “O” where the indicator $V_3$ possesses the maximum value is formed are presented in Figure 5. Formation of this point depends on correlation between two indicators – quantity of shares held by the opponents of the issue put to a vote ($Z$) and maximum quantity of shares that may be redeemed by the company in case of established net assets and repurchase price ($A$).

In is formed under the following conditions:

$Z \leq 16.7\%$

$Z \leq 83.3\% - 4/3A\%$

If the point “O” is absent, the straight line “B” shall be located not lower than the point “C”. This situation occurs if $C \geq K$ and $B \geq C$.

The inequality $C \geq K$ can be transformed into the following inequality:

$Z \geq N/6 + 1/3$.

A fractional part of a share can be neglected as that not influencing the result. This allows expressing the inequality in percent:

$25\% \geq Z \geq 16.7\%$.

The inequality $B \geq C$ can be transformed into the following inequality:

$Z \leq 1/3N - 1/3A$ or $Z \leq 33.3\% - 0.33A\%$

Figure 6 shows a set of combinations of $V_2$ and $V_3$ whereby the indicator $V_3$ assumes the minimum value at the point “C”. Formation of this point also depends on correlation of two indicators, such as the quantity of shares belonging to those who are against the issue put to
vote \((Z)\) and the maximum quantity of shares which may be redeemed by the company in case of current net assets and repurchase price \((A)\).

This happens under the following conditions:

\[
25\% \geq Z\% \geq 16.7\%
\]

\[
Z\% \leq 33.3\% - 0.33A\%
\]

Other correlations of values \(C\), \(K\) and \(B\) provide an empty set of solutions, i.e. they are meaningless.

Recall the objectives pursued by a majority shareholder. He uses assignment of a portion of his shares to “partners” in order to reduce the quantity of shares which may be redeemed from minority shareholders, i.e. saving of costs subject to payment to dissenting minority shareholders. This is achieved through reduction of a share fraction of minority shareholders in the total quantity of shares presented for redemption.

\(F_1\) is the fraction of minority shareholders in the total quantity of shares presented for redemption. It is expressed as an \textit{objective function}:

\[
F_1 = \frac{Z}{V_1 + V_2 + Z}
\]

The task is limited to determination of minimum of the function \(F_1\) in case of constraints (1):

\[
F_1 = \frac{Z}{V_1 + V_2 + Z}
\]

The minimum of this function is reached upon achievement of maximum of the following function:

\[
F_2 = V_1 + V_2 \rightarrow \max \text{ or } F_2 = V - V_3 \rightarrow \max \text{ which is equivalent to solution of the task for minimization of the following objective function:}
\]

\[
F = V_3 \rightarrow \min
\]

in case of constraints (1) stated above.

As shown on Figure 5 above, the objective function \(F = V_3 \rightarrow \min\) assumes its minimum value at the point “O” which has the following coordinates:

\[
V_2 = (K - C)/4
\]

\[
V_3 = (3K + C)/4
\]
Figure 6 shows that the objective function $F = V_3 \rightarrow \min$ assumes its minimum value at the point “C” which has the following coordinates:

$V_2 = 0$

$V_3 = C$

3. Preservation of Control over the Company by a Majority Shareholder after Completion of Redemption of Shares

One more constraint should be borne in mind. On completion of redemption of shares a majority shareholder may preserve corporate control over the company, i.e. the quantity of shares which remains with a majority shareholder shall exceed the quantity of shares of minority shareholders by at least threefold. Let us analyze whether this condition which may be expressed as follows is fulfilled:

$V_3 \geq 3(Z_1 - Z_1)$ (condition 6)

$Z_1$ is the quantity of shares actually redeemed from minority shareholders. It may be expressed with the following formula:

$Z_1 = N/(V_1 + V_2 + Z)$

If using conditions (2) and formulas (3)

$Z_1$ will be expressed as follows:

$Z_1 = \frac{ZA}{V - 1/2 + 1/4 + 1/4 + 1 - 3Z} + Z$

or

$Z_1 = \frac{ZA}{V - 3N/8 - 3N/4 + 1/4Z}$

The condition (6) will be as follows:

$\frac{3}{4} (N/2 + 1/Z) \geq 3(Z - \frac{ZA}{V - 3N/8 - 3N/4 + 1/4Z})$

or
\[
\frac{3}{4} \left( \frac{N}{2} + 1 \right) - \frac{9}{4} Z \geq -\frac{3ZA}{V - \frac{3N}{8} - \frac{3}{4} + \frac{1}{4} Z}
\]

Under given conditions this inequality will always be fulfilled because the left-hand side is always positive, and the right-hand one is negative.

If using conditions (2) and formulas (3), a majority shareholder will preserve control over the company on completion of redemption of shares.

If using conditions (4) and formulas (5)

\(Z_1\) will be expressed as follows:

\[
Z_1 = \frac{ZA}{V - 2Z}
\]

Then the condition (6) will be as follows:

\[
3Z \geq 3\left( Z - \frac{ZA}{V - 2Z} \right)
\]

This inequality is fulfilled in an obvious way.

If using conditions (4) and formulas (5), a majority shareholder will also preserve control over the company on completion of redemption of shares.

Introduction of the rule whereby a shareholder is not entitled to put shares for redemption which were obtained by him after the date of compilation of the list of persons entitled to participate in a Meeting into the Corporate Law will not exclude manipulations of majority shareholders aimed at reduction of costs for redemption of shares from minority shareholders who do not support adoption of specific corporate actions.

**Examples**

The general shareholder meeting with the company reorganization issue is prepared. This decision is not supported by minority shareholders, and they may submit a request for redemption of shares belonging to them. Let us determine how it is possible to minimize costs for redemption of shares from minority shareholders.
Example 1, when $Z > 16.7\% N$

- Authorized capital of JSC Shakhta comprises 8,000 shares.
- A majority shareholder owns 6,000 shares together with his affiliated persons (75% of the authorized capital).
- Minority shareholders own 2,000 shares (25% of the authorized capital).
- Net assets of JSC Shakhta comprise 160 mln rubles.
- The market value of one share according to the method of net assets ($P$) comprises 20 thousands rubles.
- $N$ is 8,000 shares.
- $V$ is 6,000 shares.
- $Z$ is 2,000 shares or 25% of the authorized capital ($Z\% > 16.7\% N$).

Determine the maximum quantity of shares which can be redeemed by the company in case of this volume of net assets and repurchase price:

- $A = 10\% NA / P = 800$ shares or 10% $N$

If all minority shareholders do not support the company reorganization decision and submit a request for redemption of shares, 800 shares in the amount of 16 mln rubles will be redeemed from them.

Prior to the date of compilation of the list of persons entitled to participate in a Meeting, a majority shareholder shall determine an excess amount of shares which he can transfer to a partner who will not participate in a Meeting ($V_1$) and a partner who will participate in a Meeting and vote “against” ($V_2$). These partners along with minority shareholders will submit a request for redemption of their shares and thus reduce the quantity of shares redeemed from minority shareholders.

Let us determine by which amount it is possible to reduce payments to minority shareholders at the expense of payments to “partners” of a majority shareholder.

If indicators $Z$ and $A$ meet the following conditions:

\[
25\% \geq Z\% \geq 16.7\%
\]

\[
Z\% \leq 33.3\% - 0.33A\%.
\]
Then optimum distribution of the majority shareholder’s shares is determined according to the following formulas:

\[ V_1 = V - 3Z \]
\[ V_2 = 0 \]
\[ V_3 = 3Z \]

In this case:

\[ 30\% \geq Z\% > 16.7\% \]

Firstly, check performance of inequality

\[ Z\% \leq 33.3\% - 0.33\% \]

It is obviously fulfilled because

\[ 25\% \leq 33.3\% - 0.33\% \times 0.1\% . \]

Therefore, optimum distribution of majority shareholder’s shares between “partners” is determined as follows:

\[ V_1 = 14,490 - (3 \times 2,000) = 8,490 \text{ shares} \]
\[ V_2 = 0 \]
\[ V_3 = 3 \times 2,000 = 6,000 \text{ shares} \]

Besides, the minimized fraction of shares which will be redeemed from minority shareholders is equal to:

\[ \frac{Z}{V_1 + V_2 + Z} = \frac{2,000}{8,490 + 0 + 2,000} \approx 0.19. \]

The minimum quantity of shares which will be redeemed from minority shareholders under the described optimum strategy of a majority shareholder comprises: 800 \times 0.19 = 152 shares.

**Example 2, when Z<16.7\% N.**

- Authorized capital of JSC Shakhta comprises 16,100 shares.
- A majority shareholder owns 14,490 shares together with his affiliated persons (90% of the authorized capital).
- Minority shareholders own 1,610 shares (10% of the authorized capital).
- Net assets of JSC Shakhta comprise 200 mln rubles.
- The market value of one share according to the method of net assets (P) comprises 12.42 ths. rubles.
- N is 16,100 shares.
- V is 14,490 shares.
- Z is 1,610 shares or 10% of the authorized capital (Z<16.7% N).

Determine the maximum quantity of shares which can be redeemed by the company in case of this volume of net assets and repurchase price:

- A=10% NA/P=1,610 shares.

If all minority shareholders do not support the company reorganization decision and submit a request for redemption of shares, all their shares will be redeemed because Z≤A. The amount of costs for redemption of shares from minority shareholders will comprise 1,610X12,420 rubles=19,996,200 rubles.

Prior to the date of compilation of the list of persons entitled to participate in a Meeting, a majority shareholder shall determine which excess amount of shares he can transfer to a partner who will not participate in a Meeting (V1) and a partner who will participate in a Meeting and vote “against” (V2). These partners along with minority shareholders will submit a request for redemption of their shares and thus reduce the quantity of shares redeemed from minority shareholders.

Let us determine by which amount it is possible to reduce payments to minority shareholders at the expense of payments to “partners” of a majority shareholder.

If indicators Z and A meet the following conditions:

Z%≤16.7%
Z%≤83.3%–4/3A%,

Then optimum distribution of the majority shareholder’s shares is determined according to the following formulas:

V1=V–N/2–1
V2=1/4(N/2+1–3Z)
V3=3/4(N/2+1+Z)
Firstly, check fulfillment of the inequality

\[ Z\% \leq 83.3\% - \frac{4}{3}A\% . \]

It is obviously fulfilled because \( 10\% \leq 83.3\% - \frac{4}{3} \times 10\% . \)

According to our conclusions, a majority shareholder distributes his shares as follows:

\[ V_1 = 14,490 - \frac{16,100}{2} - 1 = 6,439 \text{ shares} \]
\[ V_2 = \frac{1}{4} \left( \frac{16,100}{2} + 1 - 3 \times 1,610 \right) \approx 805 \text{ shares} \]
\[ V_3 = \frac{3}{4} \left( \frac{16,100}{2} + 1 + 1,610 \right) \approx 7,242 \text{ shares}. \]

The minimized fraction of shares which will be redeemed from minority shareholders comprises:

\[ \frac{Z}{V_1 + V_2 + Z} = \frac{1,610}{6,439 + 805 + 1,610} \approx 0.18. \]

The minimum quantity of shares which will be redeemed from minority shareholders under the described optimum strategy of a majority shareholder comprises: \( 1,610 \times 0.18 = 289 \) shares.

4. Novations in the Corporate Law

The Corporate Law was supplemented by the structure which excludes the possibility of any manipulation of a majority shareholder (a group of persons) with his shares for the purpose of reduction of expenses for redemption of shares from minority shareholders. If the quantity of shares presented for redemption exceeds the maximum quantity of shares which may be redeemed by the company in case of current net assets and repurchase price, redemption of shares is not performed, and the decision made by a General Meeting does not become effective.

This is a novation which relates to the procedure for termination of the public company status. The company may terminate its public status on the basis of the decision on amendments to the Articles, except for indication that it is public.

The decision on this issue is made by a General Shareholder Meeting with a majority of 95% votes of all shareholders owning company shares of all categories (types) (p. 3, Art. 7.2. of

Shareholders of the public company who voted against or did not participate in voting on the specified issue are entitled to request redemption of their shares by the company according to the rules established by Art. 75 and 76 of the Federal Law “On Joint Stock Companies”.

Decisions on the specified issue will become effective on condition that the total quantity of shares, in respect of which requests for redemption are submitted, does not exceed the quantity of shares which may be redeemed by the company with account of the constraint established by p. 5, Art. 76 of the present Corporate Law⁴ (p. 4, Art. 7.2. of the Federal Law “On Joint Stock Companies”).

5. Conclusions

The study shows that ability of a majority shareholder to transfer a portion of his shares to partners prior to the date of compilation of the list of persons entitled to participate in a General Shareholder Meeting depends on correlation of two indicators:

- Z is the quantity of shares owned by minority shareholders who are against the issue put to vote;
- A is the maximum quantity of shares which may be redeemed by the company in case of current net assets and repurchase price.

—if the specified indicators meet the following conditions:

\[ Z\% \leq 16.7\% \]  \hspace{1cm} \text{(condition 2)}
\[ Z\% \leq 83.3\% - 4/3A\% , \]

Then optimum distribution of the majority shareholder’s shares is determined according to the following formulas:

\[ V_1 = V - N/2 - 1 \]
\[ V_2 = 1/4(N/2+1-3Z) \]  \hspace{1cm} \text{(formulas 3)}
\[ V_3 = 3/4(N/2+1+Z) \]

If the quantity of shares owned by minority shareholders who are against the issue put to vote comprises less than 16.7% of the authorized capital, a majority shareholder is able to act in

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⁴ The total amount of funds directed by the company for redemption of shares shall not exceed 10 percent of the cost of company’s net assets as of the date of the decision which led to creation of the right of shareholders to request redemption of their shares by the company.
the following manner. He may assign a portion of his shares to a partner who will not participate in a Meeting \((V_1)\) and transfer the other portion to the other partner who will participate in a Meeting in order to provide quorum and vote against the issue put to vote \((V_2)\). A majority shareholder will preserve the minimum possible quantity of shares \((V_3)\). Optimum distribution of majority shareholder’s shares is determined by the formulas (3).

However, for these actions to result in reduction of the quantity of shares redeemed from minority shareholders, it is necessary that correlation between the quantity of shares owned by minority shareholders who are against the issue put to vote and the maximum quantity of shares which may be redeemed by the company is expressed in the following manner:

\[ Z\% \leq 83.3\% - \frac{4}{3}A\% . \]

A set of these combinations is highlighted by darker color on Figure 7.

\[
\begin{align*}
Z\% &\leq 83.3\% - \frac{4}{3}A\% \\
25\% &\geq Z\% \geq 16.7\% \\
Z\% &\leq 33.3\% - 0.33A\%
\end{align*}
\]

These inequalities are fulfilled on condition that \(A \leq 50.3\%\)

In this case optimum distribution of the majority shareholder’s shares is determined according to the following formulas:

\[
\begin{align*}
V_1 &= V - 3Z \\
V_2 &= 0 \\
V_3 &= 3Z
\end{align*}
\]
If the quantity of shares owned by minority shareholders who are against the issue put to vote \(Z\) is in the range of 16.7% to 25% of the authorized capital, a majority shareholder may act only in the following manner. He may assign a portion of his shares to a partner who will not participate in a Meeting \(V_1\). At the same time, the minimum quantity of shares which may be preserved by a majority shareholder \(V_3\) will be equal to the threefold value of the quantity of shares owned by minority shareholders who are against the issue put to vote.

However, for these actions to result in reduction of the quantity of shares redeemed from minority shareholders, it is necessary that correlation between the quantity of shares owned by minority shareholders who are against the issue put to vote and the maximum quantity of shares which may be redeemed by the company is expressed in the following manner:

\[
Z\% \leq 33.3\% - 0.33A\%
\]

A set of these combinations is highlighted by lighter color on Figure 7.

When analyzing the situation, we considered options of behavior of minority shareholders which are the most unfavorable for a majority shareholder. In case of an option of behavior of minority shareholders which is more favorable for a majority shareholder (presence of “phantom voters”, accounts of unidentified persons, passive behavior of minority shareholders, i.e. non-participation in a Meeting), the indicator \(V_3\) may certainly be reduced that will decrease the quantity of shares redeemed from dissenting minority shareholders even more.
6. References


