

THE COLOMBIAN SIMPLIFIED CORPORATION: A PROPOSED MODEL FOR DEVELOPING JURISDICTIONS

Francisco Reyes *

TABLE OF CONTENTS

I. INTRODUCTION	113
II. IMPACT OF THE COLOMBIAN SAS	115
III. NEW REFORMS TO THE COLOMBIAN SAS.....	116
IV. CONCLUSION	117

I. INTRODUCTION

Colombian Law 1258 of 2008 introduced the Simplified Corporation (*Sociedad por Acciones Simplificada* or SAS).¹ This type of business entity incorporated modern corporate law features such as simplified incorporation proceedings, full-fledged limited liability for its shareholders, and broad freedom of contract for the definition of housekeeping and governance rules.² The SAS's "opt-in" approach also allows for private parties to draft the most suitable simple or sophisticated agreements, including those most appropriate for micro- small- and medium-sized enterprises (MSMEs). The enabling optional provisions of Law 1258 have sparked innovation in corporate law across the country.³ Aside from the boilerplate agreements that are used by most start-ups, practicing attorneys are becoming skillful at developing new legal structures suitable for the widest range of companies. A survey conducted with law firms and sole law practitioners in the capital city of Bogotá has allowed for the identification of

* Francisco Reyes is the Colombian Superintendent of Companies and Chairman for the United Nations Commission for International Trade Law (UNCITRAL).

¹ The entity's name was taken from the French legislation enacted in 1994 concerning the *Société par Actions Simplifiée*. Additional legal provisions of the Colombian SAS were also transplanted from the French model. However, the entity also derives its inspiration from U.S. and Colombian sources. In fact, certain reforms initiated in Colombia almost 20 years ago (Law 222 of 1995), which had had a limited impact in the business community, were reviewed and incorporated within the SAS law. See Francisco Reyes, *Modernizing Latin American Company Law: Creating an All-Purpose Vehicle for Closely Held Business Entities—The New Simplified Stock Corporation*, 29 Penn St. Int'l L. Rev. 6 (2011).

² Law 1258, 5 diciembre 2008, art. 1, Diario Oficial [D.O.] (Colom.).

³ *Id.* arts. 9, 10, 19, 21.

several legal structures in which one or more SAS can be properly used for an unlimited number of business purposes.⁴

Seven years after the adoption of this new type of business entity, the SAS has become the single most important innovation in corporate law in decades.⁵ As of August 2015, more than 330,000 Simplified Corporations had been incorporated in Colombia. Even more significant is the percentage of new business entities that adopt the SAS as their form of choice. Today, more than 96% of all new incorporations are done through the SAS.⁶

The success achieved by the Colombian SAS has sparked regional and international interest. The Colombian SAS could become an export product. It is a blend of common law and civil law approaches to business associations. Instead of adhering to dogma or established tradition it reflects the economic needs of common business people and successfully offers clear and sensible solutions to reduce entry barriers, ameliorate organizational problems, and provide expedited dispute resolution mechanisms. The SAS legislation is also an attempt to deal with agency problems that are common in most countries without taking into account each jurisdiction's ownership pattern.

In fact, the innovative legal features of this type of business entity as well as its appeal as a vehicle for economic growth in developing countries has fostered a couple of harmonization initiatives. In 2011, the Legal Committee of the Organization of American States approved a proposal of a Model Law on Simplified Corporations for the Americas.⁷ The purpose of such proposed legislative model was to foster the harmonization of corporate law in the

⁴ On file with author.

⁵ Following the most progressive approach to Corporate Law, this law reduced incorporation formalities to a simple filing before the Mercantile Registry. It also streamlined costs and requirements associated with the formation and operation of boards of directors, fiscal auditors, purpose clauses, and other formalistic requirements that existed before its enactment. Law 1258 made it clear that shareholders would be shielded from any liability concerning obligations arising from the business activities of the corporation. It also reduced old-fashioned prohibitions pertaining to shareholders and managers activities and, most significantly, it reinforced an effective principle of freedom of contract. Furthermore, by applying the method of *structural transplants*, this law also introduced an innovative enforcement environment where arbitration and administrative adjudication superseded inefficient judicial procedures.

⁶ *Se acelera creación de empresas en el país*, EL TIEMPO (Enero 9, 2015), <http://www.eltiempo.com/economia/empresas/creacion-de-empresas-/15071100>.

⁷ For this reason, the Organization of American States' Legal Committee has recommended the adoption of a Model Act on Simplified Corporations for all the countries in the Americas on the grounds that it represents a "very credible case in favor of legislative reforms to permit such innovative business forms" to promote economic growth. See David P. Stewart, *Recommendations on the Proposed Model Act on the Simplified Stock Corporation*, OAS, 79th Regular Session, CJI/doc.380/11 (Aug. 2011). The OAS Legal Committee's Model Act was crafted after the Colombian Law 1258. It is not intended to serve as a partial amendment to be introduced to traditional business forms regulated in national codes and statutes. Instead, what is recommended is that the enactment takes place on a separate legislation that could be linked to the existing system.

hemisphere. The establishment of a Model Law would, in fact, aid Latin American and Caribbean countries in preparing legislation that could allow for a level playing field in the area of business associations. Furthermore, in 2013 Working Group I of the United Nations Commission for International Trade Law (UNCITRAL) was assigned to provide an enabling legal framework for small and medium enterprises (SMEs).⁸ Within such a framework, the analysis of simplified registration and incorporation were to be part of the working group's main focus.

II. IMPACT OF THE COLOMBIAN SAS

The creation of this extremely successful type of entity has changed the manner in which people do business in Colombia. The SAS has vigorously contributed to the regularization of thousands of businesses that in the absence of the benefits afforded by the new law would have remained in complete informality. It has also allowed for local and national governments to collect millions of dollars in taxes. At the same time, it has fostered an exponential growth in franchise fees charged by mercantile registries all over the country. Social security contributions as well as other payments to governmental agencies have also increased within the last five years due to this new type of business entity. Furthermore, several accounting, legal, and managing services have also flourished within the new business realities that the SAS has brought about. Even more significant still is the impact that this new form has had in the creation of new jobs. Statistical analysis suggests that the unemployment rate may have gone down after the introduction of this new type of business entity. According to statistical analysis rendered by the National Office of Corporations (*Superintendencia de Sociedades*), at least 2.5 million people all over the country are employed through the existing SAS.⁹

The Colombian SAS legislation is a simple but comprehensive legal system that governs relationships not only between shareholders and other corporate participants and outsiders, but also among the participants themselves. It is endowed with legal personality, investor ownership, and full-fledged limited liability. All these features are available to corporate participants at the outset through an expeditious incorporation system. Concerning the relationships with outsiders, the law provides a system of exceptional shareholder liability through the piercing of the corporate veil or the application of the "disregard of the legal entity" theory, although restricted to the cases of abuse or fraud.

Law 1258 of 2008 also aimed at curtailing opportunistic behavior by controlling shareholders, directors, and officers. By replacing *ex ante* directory rules by *ex post* legal standards, it has allowed for a more nuanced scrutiny of the insiders' activities. Legal standards of behavior, added to a regulation of shadow

⁸ U.N. Comm'n on Int'l Trade Law, Report of Working Group I (MSMEs) on the work of its twenty-fifth session, A/CN.9/860, p. 2 (Vienna, 19-23 Oct. 2015).

⁹ Report rendered by the Deputy Superintendent for Economic Studies, Bogotá, Sept. 2013 (on file with author).

directors, are intended to promote honest behavior in the day-to-day affairs of the corporation. In order to make these new standards workable, an innovative enforcement system has been put in place. A highly sophisticated corporate law court, in which final judgments are obtained in an average term of four months, has replaced an inefficient judicial system in which protracted litigation was the dominant feature. Therefore, this type of business entity is also intended to dramatically alter the inefficient enforcement landscape by aiding to the development of a specialized jurisdiction in which matters are rapidly resolved by proficient and honest judges. The deterring effect of decisions rendered by this jurisdiction in a short period of time has impacted the business community in an unprecedented manner.

The creation of this successful entity has changed the manner in which people do business in Colombia by making the standards more transparent, in turn making businesses more compliant with their social security and tax obligations. The SAS has contributed vigorously to the regulation of thousands of businesses that in the absence of the benefits afforded by the new law would never have been formalized. Seven years after the enactment of Law 1258 of 2008, the SAS has proven both its usefulness for entrepreneurs of all sizes and its significant contribution to economic growth. The SAS has permitted local and national governments to collect millions of dollars in taxes.¹⁰ It has also fostered an increasing growth in franchise fees charged by mercantile registries all over the country.¹¹ Social security contributions, as well as other payments to governmental agencies, have increased over the last five years thanks to this new type of business entity.¹²

III. NEW REFORMS TO THE COLOMBIAN SAS

The significant experience obtained thus far allows for a second wave of legislative reforms in Colombia. A new initiative has been launched in order to incorporate the most recent developments in corporate law. The proposal for such legal improvements is a natural follow up move, which is intended to create additional conditions for entrepreneurship and economic growth. The Colombian Government has, therefore, proposed a new bill, which includes state of the art provisions that would enhance the SAS legislation and endow this type of entity with an optimal legal framework for all types of undertakings.¹³ The underlying

¹⁰ According to a report rendered on September 2013 by the Deputy Superintendent for Economic and Accounting Matters at the Superintendence of Companies for the years 2010-2012, the SAS paid significant income taxes. In fact, the report states the following figures: \$1,311,589,000 COP for income taxes for 2010 Col. \$70,784,132,000 COP for 2011, and \$176,571,054,000 COP for 2012.

¹¹ See report rendered by the Colombian Confederation of Chambers of Commerce, March, 2015 (on file with author).

¹² *Id.*

¹³ Bill #70, Colombian Chamber of Representatives, August, 2015 prepared by the

concept of this new bill relates, specifically, to the willingness to provide a higher level of leeway to the SAS's directors and officers. The proposed provisions are intended to encourage risk taking and value creation. For this purpose, the bill is aimed at setting forth legal provisions that would shield directors and officers from legal risks stemming from frivolous or illegitimate litigation. At the same time, in order to attain an adequate level of corporate governance for the SAS, the new bill includes a careful regulation concerning fiduciary duties of care and loyalty.¹⁴ Whereas the former duty is attenuated through the application of the business judgment rule, the latter is enhanced by means of a strict regulation of conflicted transactions. The relevant provisions concerning this matter are aimed at preventing the shifting to insiders of private benefits of control. This qualitative change would allow for a more reasonable allocation of economic benefits among all the shareholders. Likewise, it is expected that in the future, minority shareholders will be able to profit from the controlling shareholders' monitoring and managerial efforts without being exposed to the exponential risk of expropriation. In this manner, the conceivable distributional effects that may stem out of a more flexible regulatory business environment will be timely hampered by the efficient application of the above-mentioned standards.

The bill also upgrades the SAS legal structure by including the possibility of directors' and officers' insurance, reimbursement of legal defense expenses, directors' liability caps, and exculpatory charter provisions.¹⁵

IV. CONCLUSION

In summation, the Colombian SAS legislation has proven to be an appropriate framework for the operation of all types of closely held companies. The law that gave rise to this business entity was the result of a combination of common law and civil law types of modern business corporations. Seven years after the enactment of Colombian Law 1258 of 2008, it seems clear that it is possible to achieve high impact changes from a relatively simple reform of outdated corporate law provisions. Through the SAS, Colombia has achieved higher levels of economic formalization, access to credit and investment, increased collection of taxes, and the creation of new jobs.

The SAS experiment may be beneficial in other countries if appropriately transplanted. It could be particularly useful in developing and emerging economies where there is an increasing need for flexible and user-friendly corporate vehicles. The success of the SAS clearly suggests that businesspeople prefer flexibility to old-fashioned, misguided paternalism. Welfare enhancement reforms such as the introduction of the SAS would require, however, breaking up path dependence and overcoming certain pressure groups and backward looking

Colombian Superintendency of Companies (Superintendencia de Sociedades, *Proyecto de reforma al régimen societario*, Bogotá, ed. Superintendencia de Sociedades, 2015).

¹⁴ *Id.* at 26.

¹⁵ *Id.* at 86, 88, 89.

legal traditions. For this purpose, it would be extremely useful to prepare and promote a model act on Simplified Corporations. An instrument such as this could serve as a starting point in legislative processes for the amendment of corporate laws, especially in developing nations aware of the crucial role of this type of business association in accessing investment and credit at a reasonable cost.

