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BOOK REVIEWS

The Derivative Action in Asia: A Comparative and Functional Approach BY DAN W. PUCHNIAK, HARALD BAUM & MICHAEL EWING-CHOW, eds. [Cambridge and New York: Cambridge University Press, 2012. xxiii + 452 pp. Hardcover: US$139.10]

Corporate structures across different jurisdictions are frequently utilised for commercial, profit-making purposes. Notwithstanding this common underpinning, there is undeniably "real" (John Armour, Henry Hansmann & Reinier Kraakman, "What is Corporate Law?" in *The Anatomy of Corporate Law—A Comparative and Functional Approach* (2009) at p. 1 [Armour]) divergence in the jurisdiction-specific corporate laws that govern them. And diversity is necessary fodder for comparative scholarship, a diversity that this book unabashedly celebrates. The book presents case studies on how the derivative action operates in seven selected Asian jurisdictions. In addition, the editors author three overview chapters which attempt to draw the diverse threads together to present a coherent whole. As editors Puchniak, Baum and Ewing-Chow explain in their preface, a project which began as a quest for similarities revealed an "inconvenient truth" and that is that there is no single "grand theory" that unites the operation of the derivative action across the chosen Asian jurisdictions (at p. 90). Instead, how the derivative action functions in the different jurisdictions profiled can be accurately understood only if the multiplicity of local factors in each jurisdiction is duly considered and analysed. However, the book is itself necessarily predicated on a legal convergence, albeit admittedly a broad one—a convergence that is manifested in the governance strategy adopted by the corporate laws of the different jurisdictions: the conferment of a litigation decision right on minority shareholders. Indeed, comparative studies in corporate law are often informed by the "impressive" (Armour at p. 1) underlying uniformity of the corporate form, and the laws that govern it. As Armour, Hansmann and Kraakman observed, "[b]usiness corporations have a fundamentally similar set of legal characteristics—and face a fundamentally similar set of legal problems—in all jurisdictions" (Armour at p. 1). The derivative action is one such common response to a common corporate law problem.

Companies everywhere generally operate on the basis of the majority rule. This arguably democratic process works well in many situations. However, as corporate management often enjoys the support of the majority, an unbridled surrender to the rule can provide the means by which corporate wrongs engineered by management (or by the majority) go unremedied. This is where the derivative action comes in. As it confers standing on a shareholder who is not aligned with the majority to litigate

in respect of such wrongs, it provides the minority shareholder with the means to take active steps towards protecting its investment interests. It is thought that facilitating such shareholder activism will enhance corporate governance. As Professor John C. Coffee opined insightfully many years ago, "the knowledge that one is being watched and that one must justify one's actions improves the behaviour of most individuals" ("New Myths and Old Realities: The American Law Institute Faces the Derivative Action" (1993) 48:4 The Business Lawyer 1407 at p. 1425). The universality of this notion, itself engendered by the common underlying concern, birthed the "global phenomenon" that is the derivative action (at p. 1). Convergence in this respect is admitted as much by Puchniak and Baum, who, in chapter 1, provide a very useful discussion of the *common* characteristics of the derivative action. The editors do not limit themselves to a simplistic listing, but deliver an insightful overview which draws on the triumvirate of economic, historical and practical perspectives to provide the reader with more than a basic understanding of the characteristics of the action, and the challenges necessarily appurtenant thereto. Perhaps inevitably so, the economic analysis of the derivative action draws heavily from US-centric experience and studies. But as the editors rightly observe, such studies are likely to be of limited universal value given the unique nature of the US regime.

In chapter 2, Puchniak fleshes out the main thesis of the work that there is no single theory that is capable of adequately explaining how the derivative action functions in Asia. He does so by debunking three theories culled from existing research. The first, the 'reluctant Asian litigant' theory, was strongly refuted as being "turn[ed]… on its head" by the facts presented in the book (at p. 91). This conclusion may perhaps be less surprising than Puchniak will seemingly have the reader believe, as it seems natural that globalisation and hence, the consequent integration of economic activities, is accompanied by a concomitant dilution of cultural norms. The second theory allegedly claims that the common law is superior to civil law in protecting investors. Puchniak asserts that "the blunt civil/common law divide appears to be of little value in explaining or predicting how the derivative action functions in Asia" (at p. 93). Although the theory, attributed to Rafael La Porta *et al*. ("Law and Finance" (1998) 106(6) Journal of Political Economy 1113 [La Porta]) has been critiqued, (Katharina Pistor, "Rethinking the 'Law and Finance' Paradigm" (2009) 6 Brigham Young University Law Review 1647), this reviewer wonders if the basic concept behind the theory, that legal origins matter, may not have been too perfunctorily dismissed. Indeed, the La Porta research drew a distinction between the *existence* of laws which provide protection for shareholders and creditors, and the quality of the *enforcement* of these laws. As the derivative action is essentially a procedure for enforcement of duties owed to the company, would the underlying laws defining these duties have a measurable impact on the efficacy of the action? In chapter 1, Baum and Puchniak attribute the scarcity of the derivative action not only to the intractable incentive problem that plagues derivative actions generally, but also to the "high probability that the derivative action will fail" (at p. 21). It is not immediately apparent why failure of the action should be so prevalent, and whether the substantive law of duties has a part to play. Some consideration of this issue might be useful.

The third theory, which Puchniak has dubbed the "grandest of all theories", is one that has been increasingly applied to many areas of corporate law (at p. 93). This is the economic theory of the rational shareholder which posits, broadly, that economic

actors, including shareholders, will act with perfect rationality to maximise their overall welfare or utility. Many legal rules can indeed be analysed and evaluated on the basis of the theory. However, this economic analysis of the law is not without detractors, (Charles A.E. Goodhart, "Economics and the Law: Too Much One-Way Traffic?" (1997) 60(1) The Modern Law Review 1) and a valid criticism is the fact that human actors do not always act rationally and may, not infrequently, be motivated by non-pecuniary matters. Indeed, this is borne out by the findings in the case studies. As Puchniak reveals, it appears that non-economic, in particular political, motives are the primary drivers of derivative litigation in all the Asian jurisdictions surveyed, with the exceptions of Singapore and Hong Kong.

Apart from a final concluding chapter, the rest of the chapters are jurisdiction-specific and provide not only carefully researched coverage of the legal framework for the operation of the derivative action in each country, but also insightful analysis of the socio-political background within which the legal system functions. These chapters provide an absorbing repository of information presented in a highly readable fashion. Given that many of the selected jurisdictions have legal material that is non-English, the effort must have been Herculean indeed. The chapter on Japan, for example, impresses with an intriguing account of the limitations of economic analysis, at least in the Japanese context. This is supported by original research that is based on empirical data. The chapter on China is informative in its historical account of the recent development of corporate governance and the chapter on Singapore is a wide-ranging chapter that considered not only the derivative action itself, but also its relationship with the statutory remedy for oppression. The authors also provided a fine account of the historical development of minority shareholder protection in Singapore, although a minor inaccuracy is the assertion that there is no equivalent to s. 216(2)(c) of the Singapore *Companies Act* (Cap. 50, 2006 Rev. Ed. Sing.) in UK's *Companies Act 2006* (U.K.), 2006, c. 46 (at p. 349). An equivalent does appear to exist at s. 996(2)(c).

The book does plug a gap in existing comparative literature on the derivative action. As the editors point out, research in this area has been generally westward looking. In weaving a tapestry of Asian diversity in the area, the editors have put together a book that will undoubtedly be welcomed by all who are interested in corporate governance generally and in shareholder rights specifically.

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