



# Redemption of Minority Shares and Related Fair Price Determination in the Finnish Legal System

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## Abstract

*The Finnish Limited Company Act includes many situations where a redemption of a share is possible. However, this article focuses on examining situations where a redemption of a share results from a concentration of control in a company by a single party and analyze how the redemption price is determined. This is because the regulation in Chapter 18 of the Finnish Limited Company Act on the redemption of shares on the basis of a concentration of control is unclear. Finnish Limited Company Act determines that the price to be paid out for redemption of a share must be “fair price”. Therefore, the meaning of fair price becomes a central issue to be discussed. It identifies factors and specific reasons influence the formation of the fair price in some of the situations that may come in question. The subject is mainly approached from a legal perspective, but also from an economic theoretical point of view. This article also presents a number of different share valuation methods and how they should be used to determine the fair price. Legal argumentation and interpretation are developed based on legislation, government proposals (draft of Act), and case law, since they provide a framework for the valuation process. However, the final conclusion of the article suggests that there is no unambiguous answer as to what constitutes a fair price, as its determination depends on many variables.*

**Keywords:** Company; Fair price; Finnish Limited Company Act; Minority share; Share redemption

## 1. INTRODUCTION

A share redemption generally refers to a situation where the redeemer takes the share by force.<sup>1</sup> The *Osakeyhtiölaki*, Finnish Limited Liability Company Act (624/2006), hereinafter referred as “LCA”, defines various situations in which a share redemption may become into question. Such situations may arise when a limited company is either merged into another company or split into two or more companies. In both situations, shareholders must be given the opportunity to oppose the merger or division decision at the general meeting that decides on it and to demand the redemption of their shares or of the consideration for the division, as the case may be.<sup>2</sup> The redemption of shares may also occur, for example, on the basis of a clause in the shareholders’ agreement, or where a shareholder has

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<sup>1</sup> Ville Pönkä. *Osakeen lunastaminen: osakeyhtiö- ja sopimusoikeudellinen tutkimus*. 1<sup>st</sup> edition (Helsinki: Talentum Media, 2015), 89.

<sup>2</sup> In a merger situation under Chapter 16 of the LCA, a shareholder may demand redemption of shares, while in a division situation under Chapter 17 of the LCA, a shareholder has the right to demand redemption of his or her division consideration, but despite the term “has the right”, it is about forceful redemption, since once the redeemer makes his or her claim, the redemption can not be avoided.

abused his or her influence.<sup>3</sup> The LCA provides for an ultimate remedy in case a shareholder abuses his/her powers intentionally that is contributing to a decision that violates the standard of equal treatment or otherwise breaches LCA or the company's articles of association, then the shareholder may be imposed a duty of redemption, on the basis action brought by another shareholder.<sup>4</sup> Such mechanisms have been created to allow the shareholder to exit the company when a significant change occurs in the company which may affect the shareholder's position and influence in the company.

The purpose of this article is to examine situations where a redemption is the result of a concentration of control in a company by a single party and analyze how the redemption price is determined. The research method applies to this article is legalistic. It explores redemption rules for the redemption of minority shares, since both the LCA and the *Arvopaperimarkkinlaki*, Finnish Securities Markets Act (746/2012), hereinafter referred as "SMA", together with the case law and the draft of the Act, provide a framework - albeit a somewhat imprecise one - for the redemption of shares. However, as regards the determination of the redemption price itself, the law is unclear and the draft of the Act<sup>5</sup> does not address the question of the determination of the fair price, so that the determination of the redemption price in certain situations can be challenging, to say the least. This is illustrated by the fact that, according to Pönkä, the determination of the fair price is "cryptic".<sup>6</sup> Despite this article is approached by a legal point of view, it is therefore necessary to seek support for the fair value determination from a business perspective as well. Furthermore, as regards the redemption of shares by means of a takeover bid within the meaning of the SMA, it should be noted that the fair value is set at the price offered in the takeover bid, but that the law provides for the possibility of deviating from this price for specific reasons, and thus the way these reasons affect the formation of the fair price is an interesting subject to examine.

The article is structured as follows: first, the standard basis for the redemption of shares as defined in the LCA is discussed, followed by the standard basis for a takeover bid under the SMA. It then moves on to analyze the issues related to the valuation of the redemption price and the actual questions that the essay seeks to answer. These are (a) what is meant by fair price in LCA Chapter 18:7 and (b) what factors influence the formation of the fair price as defined in LCA 18:7 and (c) how specific reasons influence the formation of the fair price in LCA 18:7.2-3 situations. Academic concern on Finnish Company Law generally discusses compliance

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<sup>3</sup> Pönkä, *op.cit.*, 98-102.

<sup>4</sup> See Klaus Ilmonen and Kauri Marjamäki, "Corporate Governance Laws and Regulations Finland 2021-2022," International Comparative Legal Guide, 26 August 2021, <https://iclg.com/practice-areas/corporate-governance-laws-and-regulations/finland>

<sup>5</sup> In addition to the legal provisions, the draft of the act (also referred as "government's proposal") also contain the reasons behind the enactment of the law, which cannot be found in the law itself.

<sup>6</sup> Pönkä, *op.cit.*, 254.

and impact of law and regulation business entities,<sup>7</sup> the LCA, as the primary legal source in this article, has been elaborated on from various angles, among others, the influence of American corporate law on LCA,<sup>8</sup> the LCA as a model of the capital doctrine in the European Union (EU),<sup>9</sup> and the regulation on private limited liability companies.<sup>10</sup> The issue of minority share has also been widely studied by both economics and legal scholars from different perspectives and interests.<sup>11</sup> The topic of redemption share can be seen in some related contexts, for instance, on the issue of shareholder oppression.<sup>12</sup> Redemption of shares is not only regulated in the Finnish legal system,<sup>13</sup> as other countries' national legislation also covers the same concern that can be seen in some academic papers.<sup>14</sup> Besides Finland, some EU countries such as Austria, Belgium, Lithuania, and Portugal also require additional conditions to be met for redemption – *i.e.* both illegal/abusive actions by other shareholders/the company, as well as other grounds for the exercise of the right, are applied.<sup>15</sup> Similarly, Indonesian law recognizes a few situations in which share redemption may apply. Each shareholder has the right to require the company to buy back the shareholder's shares at fair price if the shareholder concerned does not accept the company's actions which are detrimental to that shareholder or the company. Such measures may relate, for example, to amendments to the articles of association, mergers, divisions or where the company assigns or secures assets worth more than 50% of the company's net assets.<sup>16</sup> In the United Kingdom, the

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<sup>7</sup> See for example Helena Sjögrén and Pasi Syrjä, "Regulation compliance in small Finnish companies," *International Journal of Law and Management* 57, no. 6 (2015): 649, 654, 656.

<sup>8</sup> See Ville Pönkä, "The Convergence of Law: The Finnish Limited Liability Companies Act as an Example of the So-Called 'Americanization' of European Company Law," *European Company Law* 14, no. 1 (2017): 22-28.

<sup>9</sup> Mária Patakyová and Barbora Grambličková, "Capital Doctrine in the European Union – A Lesson to Learn From Finland?," *The Lawyer Quarterly: International Journal for Legal Research* 6, no.3 (2016): 137.

<sup>10</sup> Janne Ruohonen, Lassi Salminen and Veikko Vahtera, "Governance and Steering of MOCs – Legal Perspective," *Lex Localis -Journal of Local Self-Government* 19, no. 3 (2021): 714.

<sup>11</sup> See for example Emanuele Teti and Iliaria Montefusco, "Corporate Governance and IPO Underpricing: Evidence from the Italian Market," *Journal of Management and Governance* (2021): 5, 10, 26; Filippo Belloc, "Law, Finance and Innovation: the Dark Side of Shareholder Protection," *Cambridge Journal of Economics* 37, no. 4 (2013): 863-888; and Corina Burunciuc and Halit Gonenc, "Reforms Protecting Minority Shareholders and Firm Performance: International Evidence," *Journal of Risk and Financial Management* 14, no.1 (2021).

<sup>12</sup> Gerard V. Mantese and Fatima M. Bolyea, "Shareholder Oppression Litigation—A National Perspective," *The Michigan Business Law Journal* 40, no. 3 (2020): 41, 44.

<sup>13</sup> Timo Kaisanlahti, "Minority Shareholders in the Finnish System of Corporate Governance" *Keskusteluaiheita*, Discussion Papers No. 810 (2002): 51-52.

<sup>14</sup> See for example the discussion on Redemption of share in Georgia in Khatuna Jinoria, "Main Problems of Protection of Shareholder's Rights in Georgia," *European Scientific Journal* 13, no. 31 (2017): 70-75; See also a study on the Right to demand redemption (buy-out) of shares in the European Union in European Commission, Directorate-General for Justice and Consumers, "Study on Minority Shareholders Protection: Final Report," Publications Office, 2018: 39-44.

<sup>15</sup> *Ibid.*, 44.

<sup>16</sup> International Finance Group, "Indonesia Corporate Governance Manual" Second Edition. Jakarta, 2018, 103.

redeemed shares are treated as canceled and the amount of the company's issued share capital is reduced by the nominal value of the shares redeemed.<sup>17</sup> In Cyprus, the legal framework extends the versatility to the terms of redemption and as such, redemption may occur at the option of the issuing company; at the option of the shareholder; and on the occurrence of a particular event.<sup>18</sup>

## **2. RESULT AND ANALYSIS**

### **2.1. The Legal Framework for the Redemption of Minority Shares in Finnish Limited Company Act**

#### **2.1.1. Share Redemption on the Basis of a Concentration of Control**

The redemption of minority shares on the basis of a concentration of control is legislated in the LCA, Chapter 18 of which sets the rules for the redemption of minority shares. Pursuant to 18:1 LCA:

“A shareholder with more than nine tenths (9/10) of all shares and votes in the company (redeemer) shall have the right to redeem the shares of the other shareholders at the fair price (right of squeeze-out). A shareholder whose shares may be redeemed (minority shareholder) shall have the corresponding right to demand that the shareholder's shares be redeemed (right of sell-out).”

In the application of that norm, the shares and votes held by a corporation or foundation where the redeemer exercises control and the shares and votes held jointly by the redeemer or the corporation or foundation shall be deemed to be shareholdings of the redeemer. In addition, this norm determines that any voting restrictions based on law or the Articles of Association shall not be taken into account in the calculation of the votes of the redeemer. The shares and votes held by the company itself or by its subsidiaries shall not be taken into account in the calculation of the total numbers of shares and votes in the company. Further, were there to be more than one redeemer in accordance with subsections (1)-(3), the shareholder who has the most immediate majority of shares and votes in the company, as referred to in this section, shall be deemed the redeemer.

Thus, LCA 18:1.1 sets two quantitative requirements for the right of redemption to arise; the redeemer holds more than nine tenths of all the shares of the target company and the votes attached to the shares.<sup>19</sup> Therefore, both requirements must be fulfilled simultaneously, otherwise there is no right of redemption under LCA 18:1. Once the limit of 9/10 is exceeded, the majority shareholder has the right to redeem the shares held

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<sup>17</sup> Neal Watson and Beliz Mckenzie, “Shareholders’ Rights in Private and Public Companies in the UK: Overview,” [https://uk.practicallaw.thomsonreuters.com/5-613-3685?transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://uk.practicallaw.thomsonreuters.com/5-613-3685?transitionType=Default&contextData=(sc.Default)&firstPage=true).

<sup>18</sup> Ioanna Georgiou and Demetris Achilleos, “The Mechanism of Redemption of Shares under the Cyprus Companies Law, Cap. 113,” <https://www.lowtax.net/articles/The-mechanism-of-Redemption-of-Shares-under-the-Cyprus-Companies-Law-Cap-113-596149.html>

<sup>19</sup> Manne Airaksinen, Pekka Pulkkinen and Vesa Rasinaho. *Osakeyhtiölaki II*. 3<sup>rd</sup> revised edition. (Helsinki: Alma Talent Oy, 2018), 593.

by the other shareholders at a “fair price”. Similarly, minority shareholders in such a situation have the right to demand redemption of their shares, but there is no compulsion to demand redemption on either side. Instead, the majority shareholders are under an obligation to redeem the minority shares if the minority shareholder so requests and, conversely, the minority shareholder cannot object if the majority shareholder wishes to redeem the minority shares.<sup>20</sup> For this reason, the redemption of minority shares may also be referred to as compulsory redemption, since redemption cannot be prevented if one party so requests.<sup>21</sup>

The redemption of a share on the basis of a concentration of control has a significant impact as part of the redemption procedures. The purpose of the regulation is to provide safeguards for both the majority shareholder and the minority shareholder.<sup>22</sup> For example, minority shareholders may not have the means to influence the decisions of the majority shareholder when control increases, with the result that the ability to influence the shares becomes almost non-existent. On the other hand, for the majority shareholder, the purpose of the regulation is to enable him or her to take over the ownership of the company and thereby enable him or her to develop the company and use its assets without taking into account the opinions of the minority shareholder, thus contributing to economic efficiency.<sup>23</sup> The regulation thus aims to normalize an imbalanced situation.<sup>24</sup> In this context, it is probably worth pointing out that the redemption of minority shares is not only a product of the Finnish legal system but is commonly used in Western countries and is known as “squeeze-out”.<sup>25</sup>

Often the assessment of the existence of the right to redeem is not a problem. However, the valuation of the redemption price often raises questions of interpretation, for example as to how the redemption price should be determined. For example, Seppänen has described the nature of valuation as “problem-solving and decision making in the face of uncertainty and incomplete information”.<sup>26</sup>

In principle, the parties can agree between themselves on the redemption and its terms, without having to resort to an external procedure. However, when there is a dispute either about the existence of a right of redemption or about the amount of the redemption price, the arbitration procedure of LCA 18:3, whereby the arbitrators are charged with resolving disputes concerning the right of redemption and the redemption price, is

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<sup>20</sup> Pönkä, *op.cit.*, 506.

<sup>21</sup> Hanna Savolainen and Jani Saastamoinen “OYL 18:7:n mukainen käypä hinta – tilastollinen analyysi noteeraamattomien yhtiöiden vähemmistöosakkeiden lunastushinnan määräytymisestä” *Lakimies* 2 (2016): 250, see also the reasoning for the Normet Group Arbitration award 2.9.2019, 112.

<sup>22</sup> For example, the right to demand an extraordinary general meeting or the right to demand the distribution of minority dividends.

<sup>23</sup> KKO 2012:64, para 14. KKO is an abbreviation of Finnish Supreme Court.

<sup>24</sup> Savolainen and Saastamoinen, *op.cit.*, 250.

<sup>25</sup> Ville Pönkä, “Osakkeen negatiivinen lunastushinta – Arviointia ratkaisun KKO 2020:99 valossa,” *Defensor Legis*, no. 4 (2021): 779.

<sup>26</sup> Harri Seppänen, “OYL 18 Vähemmistöosakkeiden lunastushinta: käyvän hinnan käsitteen määrittäminen,” *Defensor Legis*, no.2 (2020): 200.

used. The purpose of the arbitration is to achieve a situation where the fair price of the share corresponds as closely as possible to the actual value of the shares so that the final result can be considered fair and equitable for all shareholders.<sup>27</sup>

### **2.1.2. Mandatory and Voluntary Takeover Bids under the Securities Market Act**

The SMA contains provisions for both voluntary and mandatory takeover bids. According to SMA 11:24.1, in a voluntary takeover bid, the offer consideration may be paid either in cash, securities, or a combination of both. In addition, the offeror may voluntarily decide on the offer consideration, unless otherwise provided for in paragraphs 2 or 3 or SMA 11:7.

The mandatory takeover bid is governed by Chapter 11 of the SMA, Section 19 of which provides that:

“A shareholder, whose proportion of voting rights increases to over 30 percent or to over 50 percent of the votes attaching to the shares of the offeree company (bid threshold) after the share of the offeree company has been admitted to trading on a regulated market (party obliged to launch a bid), shall launch a takeover bid for all other shares issued by the offeree company and for securities entitling thereto issued by the offeree company.”

Similarly, the amount of the offer in a mandatory takeover bid is regulated in SMA 11:23, according to which the fair price is to be paid as offer consideration in a mandatory takeover bid. With regard to the SMA, the Act lays down more precise rules than the LCA as to what is meant by the fair price, but derogations are still possible for specific reasons.

At this point, it is necessary to make a practical distinction between the redemption of shares on the basis of a takeover bid and redemption of shares on the basis of an increase in control: in a mandatory (and voluntary) takeover bid, minority shareholders are under no obligation to accept the takeover bid, so there is no compulsory takeover.<sup>28</sup> However, if a majority of minority shareholders accept the redeemer's takeover bid and the redeemer thereby acquires more than nine-tenths of the target company's shares and the votes they carry, the party rejects the takeover bid may then be subject to a compulsory takeover. Although this article focuses on redemption from the perspective of the LCA, the above-mentioned sections of the SMA are relevant, as the redemption of minority shares under LCA 18:1.1 is an event that often follows a takeover bid.<sup>29</sup>

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<sup>27</sup> *Ibid.*, 199-200.

<sup>28</sup> Finnish Arbitration award Silmäasema Oyj, 23.6.2020, 102-103.

<sup>29</sup> See GP 6/2006 vp, 7, according to which “redemption often constitutes the last step in the takeover bid procedure.” GP is an abbreviation for Government's proposal.

## 2.2. Applicable Law for Determining the Redemption Price of a Share

### 2.2.1. Basis for Determining the Redemption Price

The determination of the redemption price is governed by Chapter 18 Section 7 of the LCA and can be seen as comprising provisions on the determination of the redemption price in three different situations. The rules for determining the redemption price combine the provisions of the LCA and the SMA<sup>30</sup> and should therefore be treated in parallel. LCA 18:7.1 contains a general provision on the amount of the redemption price<sup>31</sup> and provides that the redemption price of a share should be determined on the basis of the fair market price prior to the commencement of arbitration proceedings. The problem with this provision is the interpretation of what is meant by the fair market price.

According to the draft of the LCA, the fair price should be determined on the basis of the market price of the share.<sup>32</sup> The Government's draft emphasizes that the fair price should be determined in this way, particularly in the case of publicly traded companies, but also in the case of other companies if the market price can be considered to have been reliably established.<sup>33</sup> The problem of fair value determination often arises in the case of unlisted companies whose shares are not traded in a way that could establish a reliable, realistic market price for the share.<sup>34</sup>

LCA 18:7.2 defines what is to be considered the fair price in a situation where the redemption has been preceded by a mandatory tender offer pursuant to SMA 11:19, in which case the price offered in the mandatory tender offer is considered the fair price unless there is a special reason to the contrary. The law has thus left the possibility to deviate from the price offered in the mandatory takeover bid, but compliance with it is a strong starting point.<sup>35</sup> LCA 18:7.2 and the SMA operate in parallel in practice, which can be illustrated by the following example: Company A acquires 50% of the shares and the votes attached to them in listed Company B and is thus obliged under SMA to make a mandatory takeover bid for the remaining shares in Company B. If, as a result of the takeover bid, A acquires control of more than 40% of the shares in B and the votes attached to them (*i.e.* in total A would own more than 90% of the shares and votes), A would also have the possibility to redeem the remaining shares in B on the basis of LCA 18:1.1. In such a case, the fair price would be based on the price offered in the mandatory takeover bid pursuant to LCA 18:7.2, unless there are reasons to the contrary.

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<sup>30</sup> For example, Olli Paavola, "Lunastushinnan määrittäminen ja osingonjaon merkitys julkisen ostotarjouksen jälkeisessä vähemmistöosakkeen lunastusmenettelyssä" (Master Thesis, Faculty of Law, University of Lapland, 2021), 36.

<sup>31</sup> Pönkä, *op.cit.*, 642.

<sup>32</sup> Government's Proposal 109/2005 vp, 173, where reference is made to KKO 1993:31.

<sup>33</sup> *Ibid.*

<sup>34</sup> Hanna Savolainen, "OYL 18:7 mukaisen käyvän hinnan määrittäminen noteeraamattomissa yhtiöissä," *Edilex* 33 (2016): 2.

<sup>35</sup> Airaksinen, Pulkkinen and Rasinaho, *op.cit.*, 626.

LCA 18:7.3 concerns the right and obligation to redeem arising from a voluntary takeover bid, and according to this, when the right and obligation to redeem has arisen in a voluntary public takeover bid pursuant to Chapter 11 of the SMA and the redeemer has acquired at least nine-tenths of the shares offered, the fair price shall be the price offered in the public takeover bid, unless there are special reasons to the contrary. In this case, the starting point is that the conditions for redemption of a share according to the LCA have not been fulfilled initially, but as a result of the voluntary takeover bid: (1) the redeemer has acquired more than nine-tenths of the shares of the offeree company; and (2) the redeemer has acquired more than nine-tenths of the shares and the votes attached to them in respect of the shares subject to the takeover bid.

### **2.2.2 Fair Price according to Finnish Limited Liability Company Act**

According to LCA 18:7:1, the redemption price of the share must be valued at fair value. This is justified, first of all, because Article 15 of the Finnish Constitution provides that everyone's property is protected and that the expropriation of property for compensation is expressly regulated by law. The right of redemption of the majority shareholder can be seen in this context as having a 'coercive nature', encroaching on the property rights of the minority shareholder in a way that the minority shareholder cannot even influence in practice. There must therefore be serious grounds for such interference with fundamental rights. As regards the redemption of shares in public limited companies, it has been interpreted that the requirement of the principle of full compensation, which aims to ensure the preservation of the protection of property, is met when the redemption is valued by the usual valuation methods.<sup>36</sup> Since normal valuation methods are normally used to determine the fair value, it can then be considered as sufficient compensation for expropriation.<sup>37</sup>

In the Government's draft of the LCA, the fair market value is not defined in more detail, but its interpretation is based on the legal literature and practice that emerged during the period of the old Limited Companies Act (734/1978). The draft to the LCA states that it was not considered necessary to include in the proposal an express provision, that the arbitrators must take into account all the relevant factors in each individual case when determining the price,<sup>38</sup> but this practice is still followed. In my opinion, this has been the right solution from a legislative point of view, as the determination of the fair price often consists of so many different factors that it would be impossible to lay down an unambiguous and precise law. Another justification for the "imprecision" of the law could be that, if it were possible to write the fair price determination precisely into law, it could then undermine the purpose of arbitration and all disputes would be resolved according to a certain guideline. It has therefore been justified to leave the

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<sup>36</sup> Savolainen, *op.cit.*, 6.

<sup>37</sup> See *e.g.* Finnish Arbitration award Normet Group Oy, *op.cit.*, 112.

<sup>38</sup> Government's Proposal 109/2005 vp, 173.

provision of the law sufficiently open to allow the arbitral tribunal to take into account all the relevant factors in a particular case.

According to LCA 18:7.2, when the redemption of minority shares has been preceded by a mandatory takeover bid pursuant to SMA 11:9, the fair price shall be the price offered in the takeover bid, unless there are special reasons to the contrary. This provision of the LCA transposes the requirements of the Takeover Bids Directive<sup>39</sup> into Finnish national law. For the redemption of shares following a mandatory takeover bid, the starting point for determining the fair price is SMA 11:23.2, according to which the fair price is the highest price paid by the offeror for the securities subject to the bid during the six months preceding the obligation to make a bid. According to SMA 11:23.3, if the offeror has not traded the securities offered during this period, the starting point for determining the fair price is the average of the prices paid for the securities offered in trading on a regulated market during the three months preceding the obligation to make an offer, weighted by the trading volumes.

LCA 18:7.3 contains a similar provision on the determination of the redemption price and when the right and obligation to redeem has arisen through a voluntary takeover bid, the fair price is also the price offered in the takeover bid, unless there are specific reasons for the contrary. With regard to the offer price of a voluntary takeover bid, the SMA only provides for a takeover bid in situations where the takeover bid is made for all shares issued by the offeree company and the securities issued by the offeree company to which they are entitled. In such cases, the offer consideration is, in principle, the highest price paid by the offeror during the six months preceding the announcement of the takeover bid. However, an exception may be made for specific reasons.

### **2.2.3. Specific Reason for Deviation from the Offer Consideration Price**

The special reason for deviating from the fair price as defined in LCA 18:7.2-3 only applies in situations where the tender offer of SMA has led to a redemption situation of minority shares under Chapter 18 of LCA. This is because the fair value of the redemption right resulting from ordinary transactions does not yet exist at this stage, as it has not been determined. This means that the fair value of LCA 18:7.2-3 is, in principle, determined based on the SMA. The provision to consider the price offered in a mandatory takeover bid as the fair price has become a rather strong principle in arbitration practice, as specific reasons for deviation has only been at issue in two arbitration awards during the 2006 LCA,<sup>40</sup> so it can be

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<sup>39</sup> Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on Takeover bids, Art. 15.

<sup>40</sup> Pönkä, *op.cit.*, 690-691; see also Finnish Arbitration award Salcomp Oyj 2.3.2012, where more than three years had passed from the date of the tender offer to the date of the initiation of the arbitration and the market conditions at that time differed substantially from the conditions at the time of the initiation of the arbitration and Finnish Arbitration award Birka Line Abp 27.1.2009, where the redeemer had made two voluntary public tender offers with different contents. In both cases, the arbitral tribunal considered that there were specific reasons to deviate from the fair price assumption.

argued that the price offered in a takeover bid often constitutes the fair price and that there is a high threshold for deviating from this based on specific reasons. It can therefore reasonably be argued that there is no clear legal guidance on the special reason in the case law and that the interpretation will remain largely at the discretion of the arbitrators in the future.

The Government's Proposal for the LCA does not directly mention what is meant by special reasons. However, in assessing the existence of special reasons, attention should be paid to at least two issues:<sup>41</sup> firstly, a special reason for derogation may arise when a long period has elapsed between the launch of the takeover bid and the start of the redemption procedure. The longer the time between these two events, the less importance can be attached to the price of the takeover bid.<sup>42</sup> The reasoning behind this is that the share's price may undergo major changes between these two events so that the price of the takeover bid does not reflect the current value of the share.<sup>43</sup> The Takeover Bids Directive has considered such a period to be three months from the execution of the takeover bid to the redemption request, but the LCA does not include such a time limit.<sup>44</sup>

Second, the number of shareholders who have accepted the takeover bid is also relevant. The more shareholders who have accepted the takeover bid, the more it indicates that the offer price has been proportionate and thus indicative of the fair price.<sup>45</sup> There are no specific rules on what constitutes a sufficient number. In general, it has been held in case law that an acceptable number is an amount by which the redeemer has acquired through a takeover bid more than 50% of the shares subject to the takeover bid.<sup>46</sup>

Specific reasons for deviating from the fair value may also arise under the SMA and may also apply - albeit exceptionally - when there has been a specific change in the stock market or in the underlying company that has affected the development of the stock exchange price. In addition, a special reason may also be present if the takeover bid violated the principle of equality by paying a special benefit to the shareholder of the offeree

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<sup>41</sup> On the other hand, it is also possible that the issue is assessed on the basis of the coverage of the takeover bid, but this mainly applies to voluntary takeover bids, see Paavola *op.cit.*, 52-53.

<sup>42</sup> Government's proposal 109/2005 vp, 174; see also Finnish Arbitration award Salcomp Oyj 2.3.2012.

<sup>43</sup> See e.g. Essi Rimali "Pörssiyhtiön vähemmistöosakkeen lunastushinnan määräytyminen - käyvän hinnan määrittämisen yhtenäistymisestä osakeyhtiölaissa ja arvopaperimarkkinalaissa," *Oikeustiede-Jurisprudentia* XL(2007): 258.

<sup>44</sup> Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on Takeover bids, Art. 15.

<sup>45</sup> Government's Proposal 109/2005 vp, 174; see also Airaksinen, Pulkkinen and Rasinaho, *op.cit.*, 625-626 and Jarmo Parkkonen and Märten Knuts. *Arvopaperimarkkinalaki*. 5<sup>th</sup> revised edition (Helsinki: Talentum, 2014), 607.

<sup>46</sup> Rimali, *op.cit.*, 260-261; Juha Jokinen, "Osakeyhtiön vähemmistöosakkeenomistajien osakkeen lunastushinnan määrittäminen, erityiset syyt poiketa markkinahinnasta ja hinnanmuutoksen olennaisuus," *Oikeustieto* 2 (2009): 18-19.

company or if the intention was to circumvent the six-month time limit in Article 11:23.2 of SMA.<sup>47</sup>

It is therefore justified to argue that there is no reason to derogate from the offer consideration where the bid has been correctly priced and has therefore led to sufficient acceptance by the shareholders and where the period between the end of the offer period and the redemption procedure has not been longer than a negligible period.<sup>48</sup> This has also been stated in the arbitration award *Silmäasema Oyj*, where the arbitral tribunal found that when the time between the procedures was short and the acceptance rate of the takeover bid was high, those who did not accept the bid should not be compensated with a redemption price higher than the offer price.<sup>49</sup>

Despite what has been said above, the price offered in a mandatory (or voluntary) bid cannot always be considered an exact price in determining the fair price, and the arbitrators must in any case assess the circumstances of the case if there are reasonable grounds to believe that the price offered as consideration for the bid does not reflect the fair price.<sup>50</sup> In other words, the arbitral tribunal should first assess whether there are specific reasons to depart from the price assumption in the case at hand. If there are reasons to deviate from the price assumption in the case, the arbitral tribunal may determine the fair price based on LCA 18:7.1. If there are no special reasons to deviate from the price assumption, the fair price should be set at the price offered in the bid.<sup>51</sup>

## 2.3. Fair Price Pricing Techniques

### 2.3.1. Market Price

As noted above, the determination of the fair price is left rather open in the law and the solution to this must be sought through different valuation methods. The starting point for determining the fair price is that the fair price should correspond to the market price of the share and its primacy has been considered a rather strong principle in the legal literature.<sup>52</sup> It has been argued, for example, that when the redemption price is based on a neutral market price, such a value is then a fair and equitable representation by all unrelated parties of the actual price level of the shares to be redeemed. This is a valid argument since once the shares have been sufficiently traded, a price based on actual transactions is then considered the most reliable alternative to other valuation methods that are based on more or less subjective calculations and estimates.<sup>53</sup> The market price thus serves as an objective measure, supporting the parties' perception of the fair

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<sup>47</sup> Parkkonen and Knuts, *op.cit.*, 607.

<sup>48</sup> Pönkä, *op.cit.*, 700-701. Also, it is worth mentioning that it is still unclear what is the exact period of time that is considered to meet this criterion.

<sup>49</sup> Finnish Arbitration award *Silmäasema Oyj*, *op.cit.*, 106.

<sup>50</sup> Pönkä, *op.cit.*, 691.

<sup>51</sup> Finnish Arbitration award *Silmäasema Oyj*, *op.cit.*, 103.

<sup>52</sup> Jukka Mähönen and Seppo Villa. *Osakeyhtiö II: Pääomarakenne ja rahoitus*. 4<sup>th</sup> revised edition. (Helsinki: Alma Talent Oy, 2020), 871.

<sup>53</sup> Savolainen and Saastamoinen, *op.cit.*, 266.

price. In this way, no party is unduly favored, as the redemption process takes into account the interests of both the majority and the minority in a balanced way, thus also ensuring the principle of economic equality.<sup>54</sup>

The primacy of the market price as a valuation tool is also reflected in the fact that it is irrelevant whether the company is listed or unlisted.<sup>55</sup> What matters is whether the market price can be considered to have been reliably established.<sup>56</sup> In this context, attention can be paid, for example, to the number of transactions that have taken place. The market price is thus determined based on past transactions in the shares of the target company.<sup>57</sup> If the market price cannot be established based on the transactions that have taken place, it is necessary to resort to various methods of comparison, comparing the target company with similar companies and their financial data. The comparative methods are largely unsuitable for unlisted companies due to the fact that comparators similar to the target company are not always available<sup>58</sup> and the use of comparative methods in arbitration proceedings has been limited.<sup>59</sup> In contrast, listed companies have greater use of benchmarking methods, as the value can be determined by comparison with listed companies or by acquisition-based methods.<sup>60</sup>

However, it is unclear how to calculate a market price for an unlisted company based on market transactions, as shares in such a company are rarely the subject of transactions that could constitute a realistic market price.<sup>61</sup> According to Pönkä, particularly, in the case of thinly held closed companies, the arbitral tribunal has often concluded that no market price could have been established for the shares of the target company.<sup>62</sup> However, a market price can be established based on even minor transactions. For example, case law has stated that in an unlisted company, the market price of a share may be determined on the basis of a single transaction if a large number of shares are sold at once.<sup>63</sup> Arbitral tribunals have held that an annual turnover of more than 20% is a sufficient threshold for a reliable market price.<sup>64</sup>

The situation is often clearer when it comes to determining the market price of shares in listed companies, which are publicly traded. However, this does not mean that the price determination is completely one-sided. In general, the market price is the stock exchange price at the time the redemption request is made, but other factors may also influence the

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<sup>54</sup> Arbitration award Normet Group Oy, *op.cit.*, 113; Savolainen, *op.cit.*, 9.

<sup>55</sup> Mähönen and Villa, *op.cit.*, 871-873.

<sup>56</sup> *Ibid.*, 871.

<sup>57</sup> Savolainen, *op.cit.*, 8-9.

<sup>58</sup> *Ibid.*

<sup>59</sup> Pönkä, *op.cit.*, 665.

<sup>60</sup> *Ibid.*

<sup>61</sup> Savolainen, *op.cit.*, 2.

<sup>62</sup> Pönkä, *op.cit.*, 662.

<sup>63</sup> KKO 1993:31.

<sup>64</sup> Mähönen and Villa, *op.cit.*, 873, where the authors refer to the arbitration award Merita Oyj, 19.4.2000, 31.

market price.<sup>65</sup> It has been observed in the legal literature that the stock exchange price does not always reliably reflect the market price in cases where there has been little trading in the share and the price formation is therefore unreliable. In such cases, when assessing the market price, attention can be focused on looking at the stock market price over a longer period and assessing its evolution. On the other hand, the unreliability is also underlined by the fact that the stock exchange can undergo major changes daily.<sup>66</sup> In the case of listed companies, it should also be noted that a takeover bid often precedes the redemption of minority shares, in which case the fair price can be determined directly based on LCA 18:7.2-3 rather than relying on LCA 18:7.1, and the market price need not be determined as such but is the price offered in the takeover bid.

### 2.3.2. Yield Value

However, it is not always possible to determine the market price. In such cases, other methods of price determination are used, in which case the fair value of the share can be determined, for example, based on the earnings or net asset value. These valuation methods, which differ from the market price, are secondary valuation methods that provide additional support.<sup>67</sup> Using secondary valuation techniques, the fair value of a share is calculated by first determining the value of the company and then dividing the value by the number of shares. The difference between secondary valuation methods and market valuation is that they reflect what the company's assets consist of.<sup>68</sup> Instead, the market price reflects people's general perception of what a stock is worth, based on the supply and demand mechanism.

The determination of the rate of return is based on a calculation of future cash flows<sup>69</sup> and is, therefore, more appropriate to reflect the value of a going concern than the net asset value, *i.e.* it is based on future expectations.<sup>70</sup> It has also been considered as an upper limit to the value of a share.<sup>71</sup> However, there are several uncertainties associated with this valuation method. The first problem is that a company may have financial years in which its turnover and results differ significantly, and in which case the yield value cannot be calculated reliably. Secondly, there may be issues such as that the company has just started its operations or that there have been significant changes in its structure. Thirdly, it should be noted that there are many different ways of calculating the yield value, which can lead

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<sup>65</sup> *Ibid.*, 871-872.

<sup>66</sup> *Ibid.*, 872, where the authors state that "a one-day stock market price can generally be questioned on the basis of the fact that it is often based on more or less random values."

<sup>67</sup> *Ibid.*, 873.

<sup>68</sup> Harri Seppänen. *Yrityksen arvonmääritys*. 1<sup>st</sup> edition (Helsinki: Alma, 2017), 183.

<sup>69</sup> Savolainen, *op.cit.*, 15.

<sup>70</sup> Veikko Vahtera, "KKO 2020:99 – Vähemmistöosakkeiden lunastus ja negatiivinen lunastushinta," *Lakimies* 3-4 (2021): 671; Savolainen and Saastamoinen, *op.cit.*, 253.

<sup>71</sup> Pönkä, *op.cit.*, 261-262.

to contradictory calculations.<sup>72</sup> However, valuation, whether based on the rate of return or other valuation methods, always involves uncertainty: there would be several legitimate ‘right’ solutions, but it would be impossible to give an unambiguous value. It is therefore acceptable that a decision is made between several reasonable alternatives, within a certain margin of uncertainty.<sup>73</sup>

The use of a yield value is mainly appropriate when the company is profitable or at least can be expected to be profitable in the future. In addition, in legal literature and arbitration practice, it has been considered in most cases to be the preferred valuation method over substantive value when the company is expected to continue its operations.<sup>74</sup>

### **2.3.3. Substantive Value**

The net asset value or substantive value is obtained by deducting the company’s liabilities from its assets. However, the net asset value of a company cannot usually be used to determine the fair value of an operating company because it only takes into account the real assets of the company.<sup>75</sup> The net asset value can be further divided into two subcategories, the net asset value of the operating company and the liquidation value. The first is where the assets of the target company consist mainly of property. This method of valuation is problematic in the sense that it would allow the company to be valued only in terms of tangible assets, without taking future prospects into account.<sup>76</sup> This is problematic for a going concern because a company may often have, for example, significant customer relationships or an established brand that could have great potential for future development. On the one hand, asset valuation has the advantage of providing an accurate picture of the value of the company’s assets at the time of the valuation, whereas income valuation is largely based on assumptions and calculated future prospects. Net asset value, on the other hand, is considered to be the value that would be obtained if the company were to cease trading and its assets were sold and is therefore mainly suitable for use in the case of a company in liquidation.

The net asset value is seen as the lower limit of the value of a share, so it effectively acts as the opposite of the return value in the “price scale” of the share, between which the fair price should seek to be derived. It can be argued, that the use of such a scale is justified from both sides of the argument. The minority shareholder is likely to want to obtain the best possible redemption price for his or her share and, conversely, the redeemer is motivated to pay as little as possible for the share.

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<sup>72</sup> Savolainen, *op.cit.*, 16. It should be noted that the calculations provided by the parties may in any case differ considerably.

<sup>73</sup> *Ibid.*

<sup>74</sup> See e.g. Finnish Arbitration award Normet Group Oy, *op.cit.*, 116.

<sup>75</sup> Savolainen, *op.cit.*, 21.

<sup>76</sup> *Ibid.*

It is also possible that the net asset value may exceed the income value in some cases.<sup>77</sup> This may be because, for example, the company has a large number of fixed assets but has been making losses for a long time. In this case, the net asset value should outweigh the yield value,<sup>78</sup> since the company would have at least this value if all its assets were liquidated. In such cases, the share's net asset value can also be used to determine the fair value of the operating company.

Another point to note about the valuation principles is that they are often used in parallel. For example, when determining the market price, aid can be sought on the basis of intrinsic or output values. Moreover, the fair price assumption created by the bid price may be corrected in this way by combining and comparing the substance and yield values.<sup>79</sup> This approach should ultimately produce the most justifiable solution.

### 3. CONCLUSION

The study first examined what is meant by the redemption of minority shares in Chapter 18 of the LCA and what is its normative basis. It also examined how the redemption price is determined and how the determination of the fair value of the redemption price depends on whether the redemption was preceded by a mandatory or voluntary offer under the SMA or by a situation where the shares were acquired by ordinary transactions.

Thus, the article found a close link between the SMA and the LCA with regard to the redemption of minority shares. In addition to that, it can be concluded that the determination of the fair price of the redemption price depends on the event preceding the redemption; if it is based on a concentration of control and a provision of more than 9/10 of the shares and votes, the fair price according to LCA 18:1.1 should be determined primarily based on the market price, regardless of whether the company is unlisted or listed. If a reliable market price cannot be determined, support must then be sought from secondary valuation methods, such as yield value, substantive value, and a combination of these. If, on the other hand, a redemption situation has been reached as a result of a mandatory or voluntary takeover bid within the meaning of the SMA, LCA 18:7(2) or (3) applies in principle, depending on the content of the takeover bid. In this case, the fair price is in principle the price offered in the takeover bid, but this may also be deviated from for special reasons and, in addition, valuation methods may be relevant if the fair price has to be adjusted.

That said, the conclusion that can be drawn from the study is that there is no unambiguous answer as to what constitutes a fair price, as its determination depends on many variables, whether it is a listed company or an unlisted company. The current state of the law does provide a framework for deciding how a fair price should be determined, but it leaves much to be

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<sup>77</sup> Pönkä, *op.cit.*, 261-262; Savolainen, *op.cit.*, 22.

<sup>78</sup> Savolainen and Saastamoinen, *op.cit.*, 267.

<sup>79</sup> Rimali, *op.cit.*, 256.

interpreted by the arbitral tribunal and possibly subsequent courts. The current situation is such that many different values can be derived for the fair price, all of which would be “fair” in themselves. Thus, the current regulation leaves an open field for the determination of the fair price, where different valuation methods should be used to find the fair price that is the ‘fairest’ of all and thus does not give an unfair advantage to the redeemer or the minority shareholder being redeemed.

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