

## Corporate Governance and Vulnerability of Minority Shareholders: An Analytical Study

Ali Raza Laghari<sup>1</sup>, Shabana Kausar<sup>2</sup>, Muhammad Nouman Jatoi<sup>3</sup>

<sup>1</sup>\* Assistant Professor, Institute of Law, University of Sindh, Jamshoro, Sindh, Pakistan.

<sup>2</sup>Lecturer at Institute of Law, University of Sindh, Jamshoro, Sindh, Pakistan.

<sup>3</sup>Civil Judge and Judicial Magistrate, MTMC III, Tando Allahyar, Sindh, Pakistan.

**Corresponding author:** [aliraza.laghari@usindh.edu.pk](mailto:aliraza.laghari@usindh.edu.pk)

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*This study reviews the corporate governance in Pakistan with more focus on the issues of minority shareholders. Due to various flaws including weak regulatory framework, dominancy of the majority shareholder and inadequate enforcement mechanism minority shareholder feel themselves unsecure with regard to their investment. To run the affairs of corporate sector a system of rules, practices and processes is called as corporate governance. A framework balancing the interests of the company's stake holders and helping to build trust in the business environment is established under the corporate governance. Enhancing the trust of investors, accountability, fairness and transparency in the affairs should be essence of the corporate governance. Doctrinal methodology has been applied in this research paper which was sufficient and satisfying to reach a conclusion. In this regard relevant laws, regulations and judicial decision were analyzed and in pursuance of this gaps and inconsistencies have been identified. It appeared that there are various flaws in the corporate governance in Pakistan consequently increasing dominancy of the majority shareholders and reducing the trust of minority shareholders. There is immediate need that Government should pay attention to this and take appropriate measure. In view of the discussion and result for the development of corporate governance and economic growth certain recommendations based on a set of reforms has been suggested.*

## 1. Introduction

In any country a system of rules, practices and processes providing a mechanism to run the affairs of a company is called corporate governance. It provides mode of operating a company, ensuring accountability, fairness and transparency in the relationship of company and its stakeholders including shareholder, management and others. For functioning and sustainability of the business, role of corporate governance is very crucial. Registered Company is the most common type of company (Ali., 2015).

A framework balancing the interests of the company's stake holders and helping to build trust in the business environment is established under the corporate governance (Azmat., 2025). Efficient, ethical and in compliance with laws and regulations the operation of the companies is considered as good corporate governance (Khan, 2022). It mitigates risks and enhances confidence of investor. Corporate Governance should be based in view of the international requirements with the principle of justice, fairness, accountability, transparency, disclosure, and responsibility ensuring all stakeholders' rights, including the share holders' rights (Hassan, 2022). In today's global economy to foster economic growth and to maintain competitive advantage effective corporate governance is essential (Wati, 2021). Actually, corporate governance means a successful corporate performance setting a business strategy. Comprehensive corporate governance laws providing management, control and protection of the rights of shareholders adopted by the advanced countries is the reason of their success (Dawood, 2023).

Interests of the shareholders in any company are protected through provided mechanism under corporate governance (Shoukat, 2025). In Pakistan in order to promote and develop corporate sector, to bring modern technological advancements into in regulatory compliance and to facilitate rapid corporatization Companies Act 2017 was promulgated. However, realities do not meet with the intention of legislature. From the analysis of the Act and other relevant literature it appears that though several progressive compliance requirements have been introduced; minority shareholder are acutely vulnerable to majority overreach and systematic wealth expropriation (Reddy, 2022). Keeping minority capital subject to the whims of controlling syndicates depresses market capitalization and discourages retail participation and stifles the broader economic formalization. There is severe need to review the Companies Act 2017 and address the statutory loopholes, procedural flaws and inconsistencies which are rendering minority shareholder protection in Pakistan theoretical instead of substantive.

## 2. Literature Review

It appears from the corporate market structure that there is dominance of heavily entrenched family owned business groups possessing majority shares and keeping hold on management not allowing the minority shareholders involvement in the affairs of the company. Proceedings including passing resolutions and election of directors in all meetings are conducted under their implied hold. On the other hand, minority shareholders practically cannot demand for scrutiny, audit of the affairs or to have their representation at the director level. By cross shareholding network companies keep control and create a web of corporate governance leaving minority intervention impossible. Dominant shareholders act as board

members and executives making decisions in their interest and causing exploitation of minority investors. Powers to sanction inter corporate financing, soft loans and high salary packages for their favored office bearers are some of the examples of exploitation. Corporate governance should be strengthened beyond the rights and responsibilities of different stakeholders (Debayao, 2014).

To prevent exploitation and ensure protection of minority shareholder SECP has set some regulation to improve corporate governance. However, there are many distortions in the Pakistani system preventing flourishing of corporate governance. Existence of an undocumented economy discouraging transparency is an example. In addition to this lack of professional skills, ownership monopoly and structural weaknesses are hurdles in the development of fair policies. Majority shareholding owner families do not allow the involvement of the minority shareholders. Lack of knowledge and deficiencies of the system also make them weak against the exploitation (Gardezi, 2022). The country needs to focus on strengthening the enforcement mechanism in the shape of penalizing the violators of the rules and regulations (Azmat, 2025).

To safeguard the interest of minority shareholders cumulative voting system provides an opportunity to get involve their representative in the board of directors. This mechanism is used in many of the developed and underdeveloped countries. In Pakistan misuse and flawed mode of implementation for the election of directors has made cumulative voting system failed to provide remedy for the minority shareholders. By reducing the powers of the majority shareholders abuse of power can be prevented. However, distribution of power between shareholders and managers may create problems in running company smoothly and create a deadlock (Imtiaz, 2018).

Samza (2023) explored that minority shareholder in Pakistan are in vulnerable position, their rights are not respected, whereas the enforcement method is limited and remedies are not adequate. It is well known fact that families, organizations and State dominating groups keep hold on these companies they dominate board by nominating their representatives as directors. Due to having majority voting share they get decisions in accordance with their desires ignoring the rights and issues of minority investors. In such a situation derivative litigation can be appropriate remedy. Supporting this point Hassan (2022) suggested that the derivative actions should be introduced in Pakistan by an amendment to the Companies Act, 2017. It will allow the individual or minority shareholders without requisite voting rights to bring a claim against the directors and majority shareholders to hold them accountable. It is also essential to hold directors accountable to the shareholders to ensure the company is being run in a manner that provides firm value maximization. Voting requirements should be reduced or abolished from sections 256 and 286, allowing for another layer of protection for the minority shareholders. There is severe need for the imposition of effective governance reforms and their strategic implementation in corporate entities. In the corporate governance main issue exists at the level of board of directors (Shah, 2022).

Corporate governance has an important role in monitoring the management to protect the interest of company and maintains the stability of interest between the stakeholders and managers (Wati, 2021). But it is linked with multiple issues (Khan, 2022). Corporate social

responsibility and good corporate governance policies are one approach for the company to provide a favorable signal to stakeholders and the market about its future survival prospects (Wati et al., 2023). Dawood (2023) suggests that profitability generally benefits from good corporate governance.

Tahir (2012) has proposed a hybrid model for Pakistani companies consisting of (i) supervisory board and (ii) management board headed by a chairman. Fazail (2024) is of the view that modernization of corporate law in Pakistan is no longer a mere aspiration but is need of the time in global digitalization. Though certain measures have been taken in the corporate legal framework still it is not addressing digital challenges. Alignment of corporate law with digital advancement will unlock opportunities for sustainable growth. The Companies Act 2017 recognizes exceptions to corporate personality and limited liability doctrines (Ajmal., 2021). The future of justice lies in constructive, interest-based solutions and mediation is a good option (Shoukat, 2025).

Zafar (2022) has suggested to revise the corporate governance code and induct outsider directors in the board. It has also been suggested to strengthen and enhance democracy of shareholders and stake holders. Fundamental value of corporate law is that it allows market participants to build governance arrangements (KERSHAW., 2021). To fill the gap and establish new standards of corporate behavior principles and guidelines have been provided by international organizations and standard setter institutions. Non-implementation of corporate governance laws can give a serious impact on the reforms (GuidoFerrarini., 2023).

### **3. Research Methodology**

In this research paper doctrinal research methodology has been applied. It involved detailed analysis of statutes, case laws, regulations and other relevant material. As doctrinal research methodology provides a structure analysis of legal principles their application and deeper understanding of corporate governance, hence this researcher considered doctrinal research methodology more appropriate for the study of this topic. For foundational understanding of the theoretical and practical dimensions of corporate governance comprehensive review of relevant literature including research articles was conducted. Examination of statutory laws, rules, regulations, cases laws and research articles provided the understanding of corporate governance and identification of inconsistencies, legal gaps and challenges faced by the minority shareholders. Comparative analysis of the advanced and developed countries has also been prescribed to find out best practices for addressing the issues.

#### **3.1 Development and comparative analysis**

England and France have diverted the government policies toward social ends of the corporation. But it is somehow absent in USA, the capitalist approach favouring shareholders interest dominated. Pakistan followed English approach. Post-1980's era has brought new approach to company law and director's duties (Iqbal., 2021).

Corporate governance in advanced countries has often been violated by corporations themselves. In result of this economic crises raised and advanced countries initiated to

address corporate governance, American and English legislatures are considered as pioneers in drafting and setting rules and principles regarding formation of boards of directors, committees, independence of its members, transparency, effectiveness of internal control system, responsibility, composition, succession, audit and risk. There is also significant role of the legislation of Spain and France which includes preventing a conflict of interest, transparency of financial statements and protection of shareholders. The current corporate governance framework for Spain's listed companies accordingly comprises two differentiated tiers: (a) the binding provisions contained in the Spanish Company Law and other applicable laws and regulations, (b) the recommendations in the Good Governance Code are strictly voluntary based on the principle of "comply or explain". In Syria and Lebanon corporate governance is weak, however UAE has adopted modern legislation which is regarded as contemporary in the region and worldwide. Qatar's approach to the corporate governance framework is average. Egypt has followed an advanced step in corporate governance (Atallah, 2024).

Jicsin (2025) reveals that legal frameworks in the Horn of Africa are outdated causing difficulty in the exercise of minority shareholders rights; whereas in Turkey more protection has been provided to minority shareholders. It has been suggested to learn from the laws and institutions of other countries protecting minority rights, redefine criteria for minority shareholders, enhance minority share holders' rights and provide remedial framework and specialized commercial courts. However, Reddy (2022) suggests that after three decades now UK Corporate Governance Code should be abolished. The corporate governance structure directly affects its competitiveness. In China governance structure of State-owned proprietorship companies is of great significance (YuanQu, 2023). The concept of good corporate governance is based on the problem of separation between ownership and management within the company (Yanto, 2018).

## **4. Discussion and Result**

### **4.1 Minority shareholder, their rights and violations**

In Companies Act 2017 minority members have been defined as those members holding not less than ten percent of the equity share capital of a company. To receive share certificates, transfer of shares, participate in the general meetings and to receive dividend are the rights declared in the Act afforded to all shareholders regardless of their equity percentage. According to Companies Act existing members will be entitle to purchase shares in proportion to their holding shares when a company proposes to increases its subscribed capital. To encourage minority participation in the election of Directors and other special business matters through law; members have been made entitled for e-vote and postal ballots for specific corporate actions. Under the Companies Act 2017 shareholder have also been granted right to inspect the register of members, directors and other officers and minutes of the general meetings. Act requires the company to pay dividend amount through electronic mode directly in the bank accounts of shareholders.

## 4.2 Vulnerability of minority shareholder, remedy and *Foss v Harbottle* Rule

In the Companies Act 2017 of Pakistan section section 286 governs the prevention of exploitation by allowing the ten percent shareholders to invoke the Court's equitable jurisdiction. However, ten percent threshold is immaterial if the petitioner fails to prove the conduct of controlling majority cognizable oppression or mismanagement. It has been held by court that oppression provisions cannot be invoked merely to settle personal scores, resolve internal rivalries (CLD 2013, Page 1263). Petitioner must prove that the majoritarian conduct is so egregiously unlawful or oppressive that the corporate entity deserves to be liquidated by the State (CLD 2021). But in JCM No. 38 of 2024 High Court of Sindh declared that the statute is a shield against majoritarian executive abuse, not a general dispute resolution tool (JCM 38, 2024).

Companies Act 2017 has failed to provide limitation for filing oppression and mismanagement petition undermining the efficacy of Section 286 as because corporate defendants frequently and aggressively invoke Article 181 of the Limitation Act. Article 181 acts as a residual clause, imposing a strict three-year limitation period on any applications for which no specific timeline is otherwise provided in the law. If the company courts rigidly apply the three-year limitation period mandated by Article 181, minority shareholders are permanently barred from seeking redress, restitution, or judicial investigation into historical, yet highly damaging, financial misconduct that may have commenced five or ten years prior but only recently became evident in the financial statements. However Supreme Court has recognized the doctrine of a "continuing cause of action"—establishing that where oppressive conduct yields ongoing, continuous consequences, the clock on the limitation period continuously resets—the lack of an explicit statutory exemption from limitation periods introduces a massive layer of legal uncertainty (SCMR 2023). The most extreme statutory remedy against the majoritarian abuse is to apply for winding up of the company under Section 301. However, seeking a winding-up order under Section 301 frequently destroys the very economic value the minority investor is attempting to salvage. Compulsory dissolution is effectively a corporate death sentence.

Derivative action has sufficient relevance to merit independence existence (Reiseberg, 2005). Due to absence of derivative action mechanism in the Companies Act 2017 of Pakistan corporate courts rely on common law principles inherited from 19th-century English jurisprudence, most notably the foundational doctrine established in the 1843 case of *Foss v Harbottle*. In this case by declining to interfere at the behest of a minority it was required that (i) only company can file a suit against the wrong committed to it and (ii) in case of wrong relating to transaction majority shareholders may ratify it. Consequently, individual minority shareholders in Pakistan are barred to sue directors for negligence, breach of fiduciary duty, or self-dealing. To successfully establish "fraud on the minority" and bypass the *Foss v Harbottle* barrier in Pakistan, a petitioner must definitively prove not only that a severe financial wrong was committed against the company, but also that the wrongdoers hold absolute, unassailable voting control and are actively, maliciously utilizing that control to prevent the company from seeking justice. In the situation of corporate restructuring, mergers, amalgamation, acquisitions and takeovers rights of the minority shareholders are

compromised by manipulation of corporate valuations and the deliberate suppression of transparent market price discovery.

## 5. Conclusion and Recommendations

From the above literature and discussion, it appears that though Company Act 2017 provides some advantages it has failed to protect minority shareholders facing majoritarian exploitation. Structural dominance of concentrated family and State-owned block-holders remains entirely unchallenged by the rule of law. Until the loopholes are decisively closed through targeted legislative action, minority shareholder protection under the Pakistan Companies Act 2017 will remain a profound illusion and may cause adverse effects on domestic and foreign retail investment. In order to make corporate legal framework of Pakistan based on equity, accountability and protection, incorporation of legislative and institutional reforms are imperative. In this regard following recommendations are suggested.

- i. Institutional measure should be taken to ensure the balance of power and to protect the interests of minority shareholders
- ii. Ten percent threshold for oppression petitions should be abolished
- iii. Derivative litigation should be allowed
- iv. Courts should be allowed to allocate a fair percentage of recovered corporate assets directly to the petitioning minority shareholders as cost.
- v. Restrictive constraints of the article 181 of limitation Act 1908 should be relaxed. The Statute must formally recognize that oppression is virtually always a continuing wrong.
- vi. SECP must actively operationalize and deeply empower specialized, extra-judicial tribunals
- vii. Globally recognised standards of corporate governance are adopted in Pakistan.
- viii. Balance of power in the management and shareholder be ensured.

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