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# The Need for a 14th Company Law Directive on the Transfer of Registered Office

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# Contents

# Summary

The freedom of establishment for companies is one of the fundamental rights enshrined in the FEU Treaty. The provisions of the Treaty set out the basis for the right and give companies the freedom to take up and pursue activities in any Member State of the EU without being discriminated. This right has been further expanded through the adoption of new company forms as well as harmonised through several company law directives. Furthermore, the ECJ (now Court of Justice of the European Union) has little by little made the scope of the freedom of establishment clearer. While the Court has confirmed that a company incorporated in a Member State may travel freely within the EU without losing its legal personality, it is relatively unestablished whether the FEU Treaty also affords companies the freedom to change their nationality by moving their registered office to another Member State.

The 14th Company Law Directive, which would regulate the matter in detail, has been underway since the middle of the 90s but was abandoned by the European Commission in 2007. The Directive would make it possible for a company to cease to be a company under the law of the home Member State and become a company under the law of the host Member State. During this procedure, legal personality is retained.

Currently, a corporation can only make an identity-preserving nationality change if there is a legal basis for doing so in the national laws of the Member States concerned or in international agreements. Additionally, due to the Cross-Border Mergers Directive, limited liability companies can effectuate the transfer by a cross-border down stream merger, i.e. the company sets up a subsidiary in the Member State to which it wants to move and then merges the existing company into this subsidiary. Finally, the transfer can be made by means of an SE, which involves conversion to an SE and a subsequent transfer according to the provisions of the SE regulation, after which the company converts back into a public limited liability company.

The Commission found that these existing alternatives reduced the need for a Directive. Furthermore, the *Cartesio* case, which at the time was about to be decided, was hoped to bring more clarity to the matter.

My conclusion is that the Commission should reconsider its decision not to proceed with the Directive, as the current alternatives to a cross-border transfer of registered office in many ways are not satisfactory. The *Cartesio* case has, in my view, only made the need for a Directive even greater, as it only deals with one particular situation and because a Directive would provide for more legal certainty. The need for a 14th Company Law Directive is not least of principal significance. If the intention of the EU is to create one single market, why not do it to the full?

# Sammanfattning

Etableringsfriheten för företag är en av de mest fundamentala rättigheterna i Lissabonfördraget. Fördragets artiklar utgör grunden för rättigheten och ger företag rätt att starta eller driva verksamhet i vilken medlemsstat som helst i EU utan att diskrimineras. Denna rättighet har ytterligare utökats genom införandet av nya företagsformer och genom harmonisering av bolagsrätten i ett flertal direktiv. Dessutom, har EG-domstolen (numera Europeiska unionens domstol) allteftersom klarlagt räckvidden av etableringsfriheten. Även om domstolen har bekräftat att ett bolag bildat i en medlemsstat får röra sig fritt inom EU utan att förlora sin status som rättspersonlighet, är det relativt oetablerat om fördraget också ger företagen frihet att byta nationalitet genom att flytta sitt registrerade säte till en annan medlemsstat.

Det 14:e bolagsrättsdirektivet, som skulle reglera frågan i detalj, har varit på gång sedan mitten av 90-talet men övergavs av Europeiska kommissionen 2007. Direktivet skulle göra det möjligt för ett företag att upphöra att vara ett bolag enligt lagstiftningen i hemmedlemsstaten och bli ett bolag enligt lagstiftningen i värdmedlemsstaten. Under detta förfarande behåller företaget sin rättspersonlighet.

För närvarande kan ett företag endast ändra nationalitet och samtidigt bevara sin rättspersonlighet om det finns en rättslig grund för detta i den nationella lagstiftningen i de berörda medlemsstaterna eller i internationella avtal. Dessutom kan aktiebolag, tack vare direktivet om gränsöverskridande fusioner, genomföra en flytt av sitt registrerade säte genom att bolaget bildar ett dotterbolag i den medlemsstat till vilken man vill flytta och sedan fusionerar in det befintliga bolaget i detta dotterbolag. Slutligen kan flytten göras genom ett SE-bolag, där bolaget först får omvandlas till ett SE-bolag och därefter kan flytta sitt säte i enlighet med bestämmelserna i förordningen, varefter bolaget till sist omvandlas till ett publikt aktiebolag.

Kommissionen fann att dessa befintliga alternativ minskade behovet av ett direktiv. Dessutom hoppades man att *Cartesio*-målet, som då var på väg att avgöras, skulle bringa mer klarhet i frågan.

Min slutsats är att kommissionen borde ompröva sitt beslut att inte gå vidare med direktivet, eftersom de nuvarande alternativen till en gränsöverskridande flyttning av det registrerade sätet på många sätt inte är tillfredsställande. *Cartesio*-domen har, enligt min mening, bara gjort behovet av ett direktiv ännu större, särskilt eftersom endast en viss situation berörs och eftersom ett direktiv skulle medföra större rättssäkerhet. Behovet av det 14:e bolagsrättsdirektivet är inte minst av principiell betydelse. Om avsikten med EU är att skapa en enda marknad, varför inte göra det till fullo?

# Abbreviations

| | |
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| AG | Advocate General (of the European Court of Justice) |
| BV | Besloten Vennootschap (NL) |
| EC | European Community |
| EC Treaty | Treaty establishing the European Community (as amended by the Treaty of Maastricht) |
| ECJ | European Court of Justice |
| EEIG | European Economic Interest Grouping |
| EU | European Union |
| FEU Treaty | Treaty on the Functioning of the European Union (as amended by the Treaty of Lisbon) |
| GmbH | Gesellschaft mit beschränkter Haftung (D, A) |
| Ltd. | Limited Company (UK) |
| Member State | Member State of the European Union |
| OJ | Official Journal of the European Union |
| PLC | Public Limited Liability Company (UK) |
| SCE | European Cooperative Society (Societas Cooperativa Europaea) |
| SE | European Company (Societas Europaea) |
| SME | Small and Medium Enterprises |
| SPE | European Private Company (Societas Privata Europaea) |
| TFEU | Treaty on the Functioning of the European Union (as amended by the Treaty of Lisbon) |
| UK | United Kingdom |
| US | United States |
| WFBV | Wet op de formeel buitenlandse vennotschappen (Law on formally foreign companies) |

# 1 Introduction

The freedom of establishment for companies is one of the fundamental rights enshrined in the FEU Treaty. The provisions of the Treaty set out the basis for the right and give companies the freedom to take up and pursue activities in any Member State of the EU without being discriminated. This right has been further expanded through the adoption of new company forms aswell as harmonised through several company law directives. Furthermore, the ECJ (now Court of Justice of the European Union) has little by little made the scope of the freedom of establishment clearer. While the Court has confirmed that a company incorporated in a Member State may travel freely within the EU without losing its legal personality, it is relatively unestablished whether the FEU Treaty also affords companies the freedom to change their nationality by moving their registered office to another Member State. The recently delivered *Cartesio* judgment may have shed new light on the matter. Interestingly enough, the 14th Company Law Directive, which would regulate the issue in detail, has been underway since the middle of the 90s but was abandoned by the European Commission in 2007. This has caused voices to rise among legal scholars, who argue for an acute need for a Directive.

## 1.1 Purpose and Outline

The purpose of this thesis is to examine the need for a 14th Company Law Directive on the transfer of registered office with a change in the applicable law. The scope of the freedom of establishment is reviewed, in *Chapter 2*, on the basis of the FEU Treaty and secondary legislation, as well as an in-depth evaluation of the case law delivered by the ECJ. Furthermore, the issue of the transfer of registered office is described in *Chapter 3*, and what the alternatives to a Directive are at the present time. The procedure resulting in the abandonment of the proposal and the position of both the European Commission and the European Parliament in the matter at hand is reviewed in *Chapter 4*. The thesis leads up to an analysis, in *Chapter 5*, of how far the freedom of establishment has come and if it entails a transfer of the registered office. The alternative methods to transferring the registered office are analysed to determine if they are adequate in order to accommodate what the 14th Company Law Directive may achieve. Finally, in *Chapter 6*, a conclusion is drawn on whether there is a need for the Directive.

## 1.2 Method and Material

In order to meet the purpose of the thesis, the traditional *legal dogmatic method* is employed, which entails the description and analysis of different sources of law. In this case, EC law sources have been used, which ranges from acts of primary and secondary law to the case law of the ECJ, as well

as reports and preparatory works from the Commission and other EU institutions. Legal literature, such as books and articles from a number of legal journals are consulted, not least for providing a basis for the analysis.

## 1.3 Definitions and Delimitations

For the sake of clarity, the Articles of the FEU Treaty will be used throughout the thesis, despite the fact that the EC Treaty was applied in all of the referred ECJ cases. The content of the Articles, however, has not been changed due to the Treaty of Lisbon[1].

In order to diversify the language, different terms are used to illustrate the same type of seat, i.e. *statutory seat*, *registered office* and *formal seat* represent the location where the company is registered. In the same way, *the real seat*, *the head office* and *the centre of administration* represent the location where the management and the administration of the company are carried out.

The term *home state* signifies the Member State where a company is registered, whereas the *host state* is the state where a company has a primary or secondary establishment.

Other definitions will be explained in the course of the thesis.

This sort of topic will inevitably touch upon numerous different areas of law, such as tax, competition, labour, company and private international law. Furthermore, national law and Community law often needs to be applied simultaneously. Thus, even if this thesis focuses on EC company law, it will also discuss limited parts of other fields of law, such as tax law and private international law.

[1] Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community, signed 13 December 2007, 2010/C 83/01.

# 2 Freedom of Establishment

The increasing establishment of companies out of the own Member State has had great significance on the enlarged European commodities exchange and the internationalisation of the markets. Provisions on the freedom of establishment can be found in the *FEU Treaty (TFEU)* and it is regulated in a number of *company law directives* on different corporate law issues. In addition, several *European company forms* have been adopted, broadening the scope of the freedom of establishment. Finally, the *case law* from the European Court of Justice (ECJ) have had great impact on the companies' right to establish freely within the EU.[2]

## 2.1 The FEU Treaty

Regarding legal persons, the basic rules on freedom of establishment are provided by Articles 49 and 54 TFEU, which are to be found under Title IV of the TFEU and have the objective to ensure the free movement of persons, services and capital.

Establishment is defined as "the actual pursuit of an economic activity through a fixed establishment in another Member State for an indefinite period"[3]. In other words, the right only concerns economic activity; there needs to be a cross-border element; and, lastly, a temporal factor is needed, which excludes short-term activities from the scope.

Article 49 TFEU is the basic provision on the right of establishment and provides:

> 'Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting up of agencies, branches, or subsidiaries by nationals of any Member State established in the territory of any Member State.
>
> 'Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 48, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the chapter relating to capital.'

Whereas the first paragraph requires the *abolition of restrictions* on freedom of primary and secondary establishment, the second provides for the right to

[2] Nilsson, M. and Lundberg, J., *Europarätten – en introduktion till EG-rätten och Europakonventionen*, p. 76.
[3] C-221/89 *R. v. Secretary of State for Transport, ex p. Factortame* [1991] ECR I-3905, para. 20.

engage in self-employed activities *on an equal footing* with the nationals of the Member State of establishment.

Article 54 TFEU provides that the freedom granted 'nationals' in Article 49 TFEU shall apply similarly to 'companies or firms', given that these are formed in accordance with the law of a Member State and have their 'registered office, central administration or principal place of business' within the Community. 'Companies or firms' include all profit-making undertakings set up under civil or commercial law and governed by public or private law.[4]

Thus, the Treaty contemplates two rights of establishment: [5]

- the right to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54 TFEU (*primary establishment*)
- the right to set up agencies, branches, or subsidiaries by nationals of any Member State established in the territory of any Member State (*secondary establishment*)

Concerning primary establishment, a company (or an individual) can exercise its right of establishment by incorporating a company in another Member State. According to Article 55 TFEU, the out-of-state company shall be treated the same way as nationals of that Member State regarding participation in the capital of the new company. A company's transfer of seat is also a type of primary establishment, even though it is rare in practice and some States forbid it. Given that a single harmonized system of company law does not yet exist throughout the Community, the solution would require, for example, Belgium to recognize a French incorporated company that chose to move all its offices, management and operations to Belgium as if it were a Belgian company but without requiring it to actually become a Belgian Company. Secondary establishment, on the other hand, is more common and it is in this area that the ECJ has been most active in eliminating obstacles to such establishment.

### 2.1.1 Exceptions from Article 49

According to Article 51, the provisions on freedom of establishment shall not apply 'so far as any given Member State is concerned, to activities which in that State are connected, even occasionally, with the exercise of official authority'. It has not been defined in Community law what 'official authority' constitutes. The ECJ, however, has stated that the provision may only be used to exempt certain activities from the right of establishment; not entire professions.[6]

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[4] Rammeloo, S., *Corporations in Private International Law – A European Perspective*, p. 27.
[5] Severinsson, D., *EG:s etableringsrätt för bolag*, p. 70.
[6] See Case 2/74 *Reyners v. Belgium* [1974] ECR 63.

Furthermore, Article 52 provides that the provisions on establishment 'shall not prejudice the applicability of provisions laid down by law, regulation or administrative action providing for special treatment for foreign nationals on grounds of public policy, public security or public health'. In other words, foreign nationals (including legal persons in accordance with Article 48 TFEU) may be refused equal treatment on grounds of public policy, public security or public health. The Council may issue directives for the coordination of the measures indicated in Article 46 (1). This has been done regarding natural persons, but in regard to companies, the derogations are governed by the Treaty and by the general principles of Community law. It is therefore up to the national courts to decide what a sufficient ground for an exception might be.

As will be shown in the ECJ case law, restrictions on the freedom of establishment can be justified by an overriding reason relating to the public interest, such as the protection of creditors, minority shareholders, employees, or fiscal interests. For national rules and measures that impose restrictions on the freedom of establishment to be justified it is necessary that they meet the terms of the so called *Gebhard-test*, which means that they are applied in a non-discriminatory manner; they are justified by imperative requirements in the public interest; they are suitable for securing the attainment of the objective which they pursue, and do not go beyond what is necessary in order to attain it.[7]

## 2.2 The Company Seat

In order to understand the case law discussed below, it is necessary to set out the terminology problems surrounding the company seat from the perspectives of national company law and national private international law.

### 2.2.1 The Company Seat in National Company Law

The company seat is first and foremost a concept of national company law. Every company are required to have a seat, which is a fundamental feature of the company. The seat allows the company to be located geographically and to be identified for the purposes of legal relations. There are two vital functions that the seat may serve; it may be the 'contact address' (formalistic function). It may also allocate the place where the 'reality' of the business is concentrated, in other words where the management and the administration of the company are carried out, where the shareholders' meetings are held, etc. (substantive function). The formalistic seat and the

[7] See C-19/92 *Kraus v. Land Baden Württemberg* [1993] ECR I-1663, para. 32, and C-55/94 *Gebhard v. Consiglio dell'Ordine degli Avvocati e Procuratori di Milano* [1995] ECR I-4165, para. 37.

substantive seat may coincide. In practice, they often do and in some legal systems, they must.[8]

For example, in English company law, the 'seat' is not a term of art, but rather the 'registered office' of a company is used, which must be located permanently in the UK. The registered office is, in reality, just an address, which must be mentioned in every company document. The formalistic seat concept is applied, which means that it is only required that it is possible for third parties to contact the company and to serve notices on the company at the given address. No further requirements are imposed, as English company law is not concerned with the economic and business reality of the company.[9]

In contrast, the French company seat, the '*siège social*' unites and serves both the formalistic and the substantive seat functions. The company seat is determined in the company statutes and must be mentioned on the stationery, invoices and all communication issued by the company. Mostly the *siège statutaire*, i.e. the seat mentioned in the company statutes, will be presumed to be the *siège social*. However, the *siège statutaire* mentioned in the statutes must reflect business reality and correspond to the company's effective place of management.[10]

To sum up, while the formalistic seat concept is a clear matter of law, the substantive seat concept is a matter of fact.[11]

### 2.2.2 The Company Seat in Private International Law

The company seat may also be a concept of private international law. Two kinds of principles, *the real seat theory* and *the incorporation theory*, are distinguished and are used to establish 'the personal statute' of companies. According to the two approaches, the link (connecting factor) between a company and its governing system of law is determined in different manners.

According to the first, *the real seat theory*, the law of the country where the company has its 'real' seat (i.e. its management and control centre) is the law applicable to company relationships. This means that the company's management is not free to choose the law which governs company law relationships. It has to be identified to which legal order the company is most closely connected, i.e. the location of the company's 'real' seat. If the formation requirements of the State where the company has its real seat are not satisfied, there are sanctions that might be applicable. Possible

[8] Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case*, p. 136.
[9] Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case*, p. 136 f.
[10] Ibid., p. 137 f.
[11] Ibid., p. 139.

consequences are the following: (i) the company as such is no longer considered to be a legal subject, and (ii) its managers are deprived of the most important company benefit, namely restricted liability.[12] The real seat theory has traditionally been applied by the private international laws of Germany, Austria, France, Belgium, Spain, Portugal, Greece and Luxembourg.

One of the positive values of the real seat theory is that nearly all possible forms of abuse of a foreign system of law by those in charge of the company's management are effectively precluded. Consequently, the real seat theory stands for equal treatment and the protection of fair competition. However, in a globalizing business world, it is often difficult to determine where a company actually has its 'real' seat. It cannot always be expected of a company to operate in only one market on a continuing basis. Furthermore, the economic mobility of companies is seriously thwarted, as cross-border transfers involve an obligatory change in the proper law of the company. The company thus risks unintended dissolution and winding-up.[13]

As opposed to the real seat theory, *the incorporation theory* bears a subjective proper law test. Following this theory, the company is governed by the law according to which it is established. The company's management is thus free to choose which legal system applies to its company law relationships. This makes the theory highly attractive for legal as well as economic reasons. It is, legally speaking, uncomplicated ascertaining the proper law since the decisive factor is of a formal nature. It is said to be the theory best suited to the common interest of accomplishing the Single Market. However, there are drawbacks of this theory as well, as opponents to the incorporation theory believe that it provokes a rat race to keep up with economic competition.[14] In Europe, the incorporation theory is used e.g. in the UK, Denmark, Sweden, Ireland, Hungary and the Netherlands.

What differs the most between the two theories is their effect on cross-border transfer of the company seat. The differences are important both from the perspective of the home state and that of the host state of the company. When it comes to the incorporation theory, it does not matter where the company's real seat is located (i.e. the law governing the existence and organisation of the company is not dependent on the location of the real seat). The real seat theory, on the other hand, attaches a different national legal order each time the real seat moves to another State, which in effect means the non-recognition of the cross-border transfer of the real seat.[15]

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[12] Rammeloo, S., *Corporations in Private International Law – A European Perspective*, p. 11.
[13] Ibid., p. 14 f.
[14] Ibid., p. 16 f.
[15] Sandström, T., *Svensk aktiebolagsrätt*, p. 31. Also see Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case*, p. 140.

## 2.3 Case Law

The following case law will chronologically give an account of how the freedom of establishment has progressed over the years. The circumstances in each case are very different and, naturally, are essential to the outcome of the case. Therefore, the cases will be described in detail in order to reflect what was definitive to the outcome.

### 2.3.1 Case 81/87 Daily Mail

In 1984, Daily Mail and General Trust PLC ('Daily Mail'), an investment holding company incorporated in the UK, wanted to transfer its central management and control to the Netherlands, whilst remaining incorporated in the UK. In principle, such a move was allowed as both Member States adhered to the incorporation theory. However, according to section 482(1) of the UK Income and Corporation Taxes Act 1970, in order for companies resident for tax purposes in the UK to cease to be so resident, consent of the Treasury was needed. Such consent may on the basis of section 482(2) be given specifically, or, if given generally, be revoked by the Treasury, and may in any case be absolute or conditional.[16]

Consequently, Daily Mail submitted an application to the tax authorities for consent under the mentioned provisions. It proposed, in particular, to hold board meetings and to rent offices for its management in the Netherlands. It subsequently decided to open an investment management office in the Netherlands, without waiting for the consent applied for.[17]

It was common ground that the main reason for the proposed transfer was to elude the obligation to pay taxes in the UK on increased capital gains after selling off the company's non-permanent assets in the UK for the purpose of using the profits to buy its own shares.[18]

Daily Mail and the Treasury did not manage to reach an agreement, which lead to proceedings before the High Court of Justice, Queens Bench Division. There, Daily Mail claimed that Articles 49 and 54 TFEU gave it the right to transfer its central management and control to another Member State without prior consent or the right to obtain such consent unconditionally.[19] The court stayed the proceedings and referred four questions to the ECJ for a preliminary ruling, of which the most important was:

> '(1) Do Articles [49 and 54 of the TFEU] preclude a Member State from prohibiting a body corporate with its central management and control on that Member State from transferring without prior consent or approval that central

[16] Case 81/87 *The Queen v. H.M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust plc* [1988] ECR 5483 (henceforth *Daily Mail*), paras. 2-5.
[17] Ibid., para. 6.
[18] Ibid., para. 7.
[19] Ibid., para. 8.

> management and control to another Member State in one or both of the following circumstances, namely where:
> (a) payment of tax upon profits or gains which have already arisen may be avoided;
> (b) were the company to transfer its central management and control, tax that might have become chargeable had the company retained its central management and control in that Member State would be avoided?'[20]

Consequently, the ECJ had to assess whether the freedom of establishment implies a right for companies to transfer their head office out of the state of incorporation and whether that right could be made subject to the consent of national authorities based on the company's tax position.

The ECJ started by emphasising that the freedom of establishment is one of the fundamental principles of the Community and that the provisions of the Treaty guaranteeing that freedom have been directly applicable since the end of the transitional period. It was also stressed that those provisions not only ensured that foreign nationals and companies are treated in the host Member State in the same way as nationals of that State, but also prohibit the Member State of origin from hindering the establishment in another Member State of one of its nationals or companies.[21]

In the view of the ECJ, the UK law at issue imposed no restrictions on transactions such as those described above, neither concerning secondary establishments, nor primary establishments. Consent from the Treasury was required only where a company sought to transfer its central management and control out of the UK while maintaining its legal personality and its status as a UK company.[22]

The ECJ noted that companies, unlike natural persons, are *creatures of the law* and exist only by virtue of the national legislation which determines their incorporation and functioning. Whereas the legislation of the Member States varies widely, the Treaty places several connecting factors on the same footing, rather than imposing common grounds for the application of the freedom of establishment on companies. Since no conventions or other coordination measures had yet been adopted by the Member States, the ECJ found that the question at hand could only be answered through an interpretation of Articles 49 and 54 TFEU, the transfer of seat being a problem which 'must be dealt with by future legislation or conventions'.[23] Thus, the ECJ held that:

> 'Under those circumstances, Articles [49 and 54] of the Treaty cannot be interpreted as conferring on companies incorporated under the law of a Member State a right to transfer their [head office] to another Member State while retaining their status as companies incorporated under the legislation of the first Member State.'[24]

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[20] *Daily Mail*, para 9.
[21] Ibid., para. 14.
[22] Ibid., para. 18.
[23] Ibid., paras. 19-23.
[24] Ibid., para. 24.

The widespread opinion is that the *Daily Mail* case should be regarded as being 'good law', even following the ECJ's recent decisions on the transfer of the administrative seat, as the ECJ distinguished the matter at issue in *Überseering* and *Inspire Art* from the issues debated in *Daily Mail*, which was therefore not overruled.[25]

### 2.3.2 Case C-212/97 Centros

Two Danish nationals, Mr and Mrs Bryde, formed Centros Ltd ('Centros'), a UK private limited company registered on 18 May 1992. During the summer of 1992, the couple wanted to establish a branch in Denmark, through which they were to carry on all their business activities. The company had never traded since its formation and the share-capital of GBP 100 had been neither paid up nor made available to the company, since UK law did not require it. The connection with the UK was limited to a registered office situated at the home of a friend of the Danish couple. Even though Centros was regarded as a foreign limited liability company under Danish law and fulfilled the conditions regarding the registration of a branch imposed on such companies, the Danish Erhvervs- og Selskabsstyrelse (the Trade and Companies Board, 'the Board') refused the registration on the ground, *inter alia*, that Centros was in fact seeking to establish in Denmark, not a branch, but a principal establishment, by evading the national rules concerning, in particular, the paying-up of minimum capital fixed at DKK 200,000 (about EUR 25,000). The decision was appealed by Centros, which claimed that, pursuant to Articles 49 and 54 TFEU, it was entitled to set up a branch in Denmark, as it was lawfully formed in the UK. The Board, on the other hand, argued that the refusal was not contrary to the said Articles since the establishment of a branch in Denmark would seem to be a way of avoiding the national rules on the provision for an the paying-up of minimum share capital. Furthermore, the Board held that the refusal was justified by the need to protect private or public creditors and other contracting parties and by the need to try to prevent fraudulent insolvencies. The case reached the Højesteret (the Danish Supreme Court), which decided to stay proceedings and referred a question to the ECJ for a preliminary ruling.[26]

In substance, the national court asked whether it was compatible with the freedom of establishment to refuse registration of a branch of a lawfully founded company that has its registered office in another member state, but in which the company does not itself carry on any business, and where the purpose of the branch is clearly to avoid the more restrictive host state rules on formation of companies.[27]

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[25] Federico M. Mucciarelli, *Company 'Emigration' and EC Freedom of Establishment:* Daily Mail *Revisited*, p. 279.
[26] Case C-212/97 *Centros Ltd v. Erhvervs- og Selskabsstyrelsen* [1999] ECR I-1459 (henceforth *Centros*), paras. 1-12.
[27] Ibid., paras. 13-14.

The ECJ ascertained that a practice of a Member State which refuses the registration of a branch of a company formed in accordance with the law if and having its registered office in another Member State constitutes an obstacle to the freedom of establishment under Articles 49 and 54 TFEU. The Board, however, meant that such measures are exempt where the sole purpose of the company's formation is to circumvent national rules governing formation of companies, i.e. an abuse of the freedom of establishment. The ECJ agreed with the Board in that Member States are entitled to take measures in order to prevent improper circumvention of national law or fraudulent reliance on Community law, but only under specific circumstances. In such circumstances, the national courts may only take account of abuse or fraudulent conducts based on objective evidence and assess it in the light of the TFEU provisions relied upon by the company.[28]

In this case, the provisions on the freedom of establishment in the Treaty shall enable companies to pursue activities in other Member States through an agency, branch or subsidiary. The ECJ found that it could not constitute an abuse of the right of establishment, if a national of a Member States wishes to set up a branch in the Member State whose rules of company law seem to him the least restrictive. Furthermore, the fact that a company does not conduct business in the Member State in which it has its registered office and pursues its activities only in the Member State where its branch is established is not sufficient to prove the existence of abuse or fraudulent conduct which would entitle the latter Member State to deny that company its right of establishment. Thus, the refusal of a Member State to register a branch of a company on the grounds that the branch is intended to enable the company to carry on all its economic activity in the host state, with the result that the branch escapes national rules on the provisions for and the paying-up of a minimum capital, is incompatible with Articles 49 and 54 TFEU, since its prevents the exercise of the right to set up a secondary establishment which Articles 49 and 54 are intended to guarantee.[29]

Lastly, the ECJ considered whether the national practice in question could be justified for the reasons submitted by the Danish authorities. The Board argued that the requirement for private limited companies to pay up of a considerable share capital was an imperative requirement in the general interest, as it pursued the objective of reinforcing 'financial soundness' of those companies to the benefit of their creditors, which could not be fulfilled by any less restrictive means.[30] The ECJ stressed that national measures liable to restrict the fundamental freedoms of the Treaty must fulfil four conditions: (1) they must be applied in a non-discriminatory manner; (2) they must be justified by imperative requirements in the general interest; (3) they must be suitable for securing the attainment of the objective which they pursue; and (4) they must not go beyond what is necessary in order to attain it. These conditions were not fulfilled according to the ECJ. Firstly, the

[28] *Centros*, paras. 21-25.
[29] Ibid., paras. 26-30.
[30] The so-called 'mandatory requirements doctrine'.

creditors of Centros were not exposed to any larger risks than if any other British company traded through a branch in Denmark. The registration of the branch would have been approved if Centros had carried out any business in the UK, according to the Danish authorities. Moreover, the ECJ held that, contrary to the arguments of the Board, it is possible to adopt measures which are less restrictive, such as different forms of guarantees. Finally, battling fraud cannot justify a practice of refusing to register a branch of a company which has its registered office in another Member State.[31] Consequently, the ECJ answered the question posed by Højesteret as follows:

> '… it is contrary to Articles [49 and 54] of the Treaty for a Member State to refuse to register a branch of a company formed in accordance with the law of another Member State in which it has its registered office but in which it conducts no business where the branch is intended to enable the company in question to carry on its entire business in the State in which that branch is to be created, while avoiding the need to form a company there, thus evading application of the rules governing the formation of companies which, in that State, are more restrictive as regards the paying up of a minimum share capital …'[32]

Centros has been hugely discussed amongst academics as the decision contrasted with the Daily Mail. However, in contrast to the Daily Mail, Centros deals with a 'moving in' scenario, where the treatment by the host state is at issue. Consequently, Centros cannot be seen as overriding the Daily Mail judgment. Another point of discussion has been whether the decision signifies an end to the real seat theory. The ECJ, however, avoided stating explicitly that the real seat theory is incompatible with the TFEU Treaty. The reason for this might have been to leave it up to the legislator to decide.

### 2.3.3 Case C-208/00 Überseering

The ECJ went further in the case with *Überseering*[33]. In 1992 Überseering BV ('Überseering'), a Dutch limited liability company, and NCC GmbH ('NCC'), a German limited liability company, entered into a construction contract. The contract involved work on German real property. Überseering sued NCC for damages because of alleged defects in the work performed. In 1994, prior to the filing of suit, two German-resident individuals, who at that time managed the company from Germany, purchased Überseering. Under German law this caused Überseering's 'actual centre of administration' to shift from the Netherlands to Germany, meaning that Überseering's separate legal existence and legal capacity depended on German corporate law.[34]

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[31] *Centros*, paras. 31-38.
[32] Ibid., para. 39.
[33] Case C-208/00 *Überseering BV v. Nordic Construction Company Baumanagement GmbH (NCC)* [2002] ECR I-9919 (henceforth *Überseering*).
[34] Ibid., paras. 1-12

Consequently, Überseering, which had not reincorporated itself in such a way as to acquire legal capacity in Germany, was, in the lower courts, refused the right to bring legal proceedings against NCC. Überseering appealed the case up to the Bundesgerichtshof, which suspended proceedings and referred two questions to the ECJ for a preliminary decision. The *first question* was, in effect, whether Articles 49 and 54 TFEU preclude the application of the law of the state where the 'actual place of administration' of a company incorporated in another Member State on the question of its legal capacity, where this application leads to the denial of the right to bring legal proceedings based on contractual obligations. If so, it was enquired in the *second question* whether Articles 49 and 54 TFEU require that the company's legal capacity and capacity to be a party to legal proceedings should be determined according to the law of the State of incorporation.[35]

The ECJ stated that since Überseering was validly incorporated in the Netherlands and had its registered office there, it was entitled under Articles 49 and 54 TFEU to exercise its freedom of establishment in Germany as a company incorporated under Dutch law. The fact that, after the company was formed, all the shares were acquired by German nationals residing in Germany, was of little significance, since it had not caused Überseering to cease to be a legal person under Dutch law. The existence of Überseering was inseparable from its status as a company incorporated under Dutch law since a company exists only by virtue of national legislation which determines its incorporation and functioning.[36] The view in Germany that any company incorporated in another Member State had to reincorporate itself in Germany to be able to bring legal proceedings was according to the ECJ 'tantamount to outright negation of freedom of establishment'. It therefore had to be determined whether such a restriction on freedom of establishment could be justified under the mandatory requirements doctrine, which was not the case.[37] Accordingly, the answer to the first question was as follows:

> '… where a company formed in accordance with the law of a Member State ('A') in which it has its registered office is deemed, under the law of another Member State ('B'), to have moved its actual centre of administration to Member State B, Articles [49 and 54 TFEU] preclude Member State B from denying the company legal capacity and, consequently, the capacity to bring legal proceedings before its national courts…'[38]

The second question was answered in the affirmative, i.e. a host Member State is required to recognise the legal capacity and the capacity to be a party to legal proceedings which a company exercising the freedom of establishment enjoys according to the law of its home Member State.[39]

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[35] *Überseering*, para. 21.
[36] As stated in *Daily Mail*
[37] *Überseering*, paras. 80-81 and 92-93.
[38] Ibid., para. 94.
[39] Ibid., para. 95.

The result of the *Überseering* case is thus that it is no longer accepted for Member States to apply the real seat theory in the stringent German fashion, with regard to companies incorporated in other Member States, but they are obligated to comply with the incorporation theory when it comes to legal capacity and the capacity to bring legal proceedings.

### 2.3.4 Case C-167/01 Inspire Art

After the *Überseering* case, the ECJ again made a decision in the *Inspire Art* case[40], dealing with the cross border transfer of the company's real seat within the EU.

Inspire Art Ltd ('Inspire Art') was a private company limited by shares, established in the UK and having its registered office there. Its sole shareholder and director was domiciled in the Netherlands. The company, which was dealing in 'objets d'art', started doing business exclusively in the Netherlands immediately after being formed. A branch of the company was registered in the commercial register of the Amsterdam Chamber of Commerce without indicating that Inspire Art was a "formally foreign company". According to a law adopted in 1997 in the Netherlands[41], such a company is subject to various obligations concerning registration, disclosure, minimum share capital, personal liability as well as an obligation to indicate its status as a formally foreign company in all documents produced by it. Inspire Art opposed to the insertion indicating its status as a formally foreign company, *inter alia* on the grounds that the WFBV was contrary to Articles 49 and 54 TFEU. The proceedings ended up in the *Kantongerecht te Amsterdam* (Amsterdam district court), which held that Inspire Art was a formally foreign company within the meaning of Article 1 of the WFBV. As regards the compatibility of the Dutch law at hand with Community law, the district court referred two questions to the ECJ. In short, it was firstly enquired whether the Articles 49 and 54 were to be interpreted as precluding the Netherlands from maintaining the requirements found in WFBV with regard to branches of companies formed in the UK only to evade the stricter Dutch rules on formation of companies and payment for shares. Secondly, was the WFBV found to be in breach of the said Articles, the district court asked if it could nonetheless be justified on the basis of Article 52?[42]

Again, the ECJ decided clearly in favour of the freedom of establishment. The rule in question, which required Dutch branches to disclose the fact that they are formally foreign companies, was ruled to be in breach of the 11th directive[43], because the latter did not permit any disclosure rules going

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[40] Case C-167/01 *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd* [2003] ECR I-10155 (henceforth *Inspire Art*).
[41] *Wet op de formeel buitenlandse vennotschappen* (WFBV)
[42] *Inspire Art*, paras. 34-39.
[43] 11th Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State.

beyond the rules contained in it. The content of the Directive was considered to be exhaustive, and a requirement corresponding to the Dutch provision could be found neither in the list of the obligatory nor of the facultative disclosure requirement and was therefore precluded.[44]

The Court also stated, recalling the reasoning in *Centros*, that the fact that a company is formed in one Member State only to conduct all of its business in another is irrelevant to the application of Articles 49 and 54 TFEU, whatever the reasons for this regime may be, save in the case of fraud.[45] Thus, the fact that Inspire Art was formed in the UK for the purpose of circumventing Dutch company law does not mean that that company's establishment of a branch in the Netherlands is not covered by freedom of establishment as provided for by Articles 49 and 54 TFEU. As the WFBV sought to impose certain conditions provided for in national law on a company exercising its right of secondary establishment, the ECJ found that there had been a restriction of the said freedom.[46]

According to the ECJ, this kind of restriction could not be justified by an imperative requirement in the public interest because neither Article 52 TFEU nor the protection of creditors, the prevention of an improper recourse to freedom of establishment, the enforcement of fairness in business dealings nor the efficiency of tax inspections could be invoked in this case.[47]

This case further ousts the real seat theory and clarifies that a foreign company is not only to be respected as a legal entity having the right to be a party to legal proceedings, but rather has to be respected as such, i.e. as a foreign company that is subject to the company law of its incorporation. It is, hence, not compatible with EU law to make any adjustment to the company law of the host state.

### 2.3.5 Case C-411/03 SEVIC Systems

The *SEVIC* case[48] dealt with the feasibility of a merger between a German company, SEVIC AG ('SEVIC'), and a Luxembourg company, Security Vision SA ('Security Vision'). The merger was planned to be realized by acquisition (or absorption), which means that without going into liquidation all the assets of Security Vision were to be transferred to SEVIC and, thus, that Security Vision would have ceased to exist. However, the competent German court rejected the registration of the merger in the national commercial register, because the law only allowed mergers by legal entities established in Germany.[49] On appeal, the regional court referred the question to the ECJ for a preliminary ruling. It was asked whether Articles

[44] *Inspire Art*, paras. 65-72.
[45] *Inspire Art*, para. 95
[46] Ibid., paras. 98 and 105.
[47] *Inspire Art*, para. 142.
[48] Case C-411/03 *SEVIC Systems AG* [2005] *ECR* I-10805 (henceforth *SEVIC*).
[49] Ibid., paras. 1-2

49 and 54 TFEU were to be interpreted as meaning that it is contrary to freedom of establishment for companies if a foreign European company is refused registration of its proposed merger with a German company in the German register of companies under German law, on the ground that that law provides only for transformation of legal entities established in Germany.[50]

The ECJ held that the German law established a difference in treatment between companies according to the internal or cross-border nature of the merger. Such a difference in treatment was regarded as constituting a restriction within the meaning of Articles 49 and 54 TFEU, which is contrary to the right of establishment and can be permitted only if it pursues a legitimate objective compatible with the Treaty and is justified by imperative reasons in the public interest. Furthermore, it is necessary that its application must be appropriate to ensuring the attainment of the objective pursued and must not go beyond what is necessary to attain it.[51]

The ECJ stated that, whilst Community harmonisation rules are useful for facilitating cross-border mergers, the existence of such rules could not be made precondition for the implementation of the freedom of establishment. It cannot be excluded that, as established by the prior rulings of the ECJ, the protection of creditor's interests, minority shareholders and employees, the preservation of the effectiveness of fiscal supervision and the fairness of commercial transactions may in certain circumstances justify a restricting national measure.[52]

The ECJ noted that the consequence of refusing generally, in a Member State, to register in the commercial register a merger between a company established in that State and one established in another Member State, is that it prevents the realisation of cross-border mergers even if the public interests mentioned above are not threatened. In any event, such a rule goes further than what is necessary to protect those interests.[53]

Consequently, the ECJ answered the referred question as follows:

> '…Articles [49 and 54 TFEU] preclude registration in the national commercial register of the merger by dissolution without liquidation of one company and transfer of the whole of its assets to another company from being refused in general in a Member State where one of the two companies is established in another Member State, whereas such a registration is possible, on compliance with certain conditions, where the two companies participating in the merger are both established in the territory of the first Member State.'

This decision has been superseded by the Cross-Border Merger Directive. Thus, the importance of the *SEVIC* decision could be doubted, but it may

[50] *SEVIC*, para. 10.
[51] Ibid., paras. 22-23.
[52] Ibid., paras. 26-28.
[53] Ibid., para. 30.

have significance beyond cross-border mergers, namely with respect to seat transfers, cross-border divisions and cross-border takeovers.[54]

### 2.3.6 Case C-2010/06 Cartesio

The latest case in the line of company law cases on freedom of establishment is the *Cartesio* case[55]. Despite the previous landmark decisions, the judgment of the ECJ was eagerly awaited as a clarification of the questions concerning the scope of the right of establishment.

Cartesio Bt. ('Cartesio') was formed in 2004 as a limited partnership under Hungarian law. Cartesio sought to transfer its registered seat from Hungary to Italy without changing the applicable law, i.e. it wished to remain governed by Hungarian law. However, the Company Court, which maintained the companies register, refused to enter the new Italian seat in the Hungarian register on the ground that the transfer was not permitted under Hungarian law. Under the Hungarian Law on the Commercial Register, the seat of a company governed by Hungarian law is to be the place where its central administration is situated. The Company Court held that a legal entity that wishes to transfer its seat to another Member State must first be wound up in Hungary and then reconstituted under the law of that Member State. The decision was appealed by Cartesio to the Court of Appeal of Szeged, which referred the case to the ECJ. [56]

Four questions were asked; the first three dealt with procedural problems and will not be discussed here. The fourth question was, essentially, whether Articles 49 TFEU and 54 TFEU are to be interpreted as precluding legislation of a Member State under which a company incorporated under the law of that Member State may not transfer its seat to another Member State whilst retaining its status as a company governed by the law of the Member State of incorporation.[57]

In its written submissions, Cartesio argued that the internal market needs an efficient solution to the necessity of relocating the seat of companies. It was the company's view that Articles 49 and 54 TFEU confer the right on a company formed in accordance with the laws of a Member State to move its seat to another Member State and demand their registration of the transfer in the national companies register. The refusal to register the transfer of seat was contended to be an unlawful discrimination between companies from different Member States based on the location of their seat, and constituted a violation of Community law.[58]

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[54] See Siems M. M., SEVIC*: Beyond Cross-Border Mergers*.
[55] Case C-210/06 *Cartesio Oktató Szoláltató bt* [2008] WLR (D) 400 (henceforth *Cartesio*).
[56] *Cartesio*, paras. 21-27.
[57] Ibid., paras. 40 and 99.
[58] Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case C-210/06*, p. 130.

The Hungarian government argued that the rules laid down in *Daily Mail* still should be considered being good law, and that Articles 49 and 54 TFEU should not be interpreted as granting a right to a company incorporated in accordance with the laws of one Member State to transfer its seat into another Member State whilst preserving the legal identity and applicable law of the state of incorporation. It was also noted that a distinction had to be drawn between the home state and the host state of the company proposing to transfer its seat. The freedom of establishment does not prohibit the home state, here Hungary, from imposing or maintaining restrictions on the cross-border transfer of the company seat. The company law of Hungary applies to companies having their seat within Hungary. If the seat is moved out of the country, Hungarian law no longer applies. Therefore, it is not contrary to Articles 49 and 54 TFEU to deny a company from keeping its Hungarian legal personality and registration in the Hungarian companies register if its seat is moved abroad. Furthermore, it was contended that if a seat transfer was declared possible under Community law, it would not be possible for national authorities to exercise any supervision over companies. Additionally, in order to protect creditors and minority shareholders as well as legal certainty the seat of a company is entitled to be situated in the country under the laws of which the company has acquired and enjoys legal personality.[59]

The response from the ECJ was as follows:

> 'As Community law now stands, Articles [49 and 54 TFEU] are to be interpreted as not precluding legislation of a Member State under which a company incorporated under the law of that Member State may not transfer its seat to another Member State whilst retaining its status as a company governed by the law of the Member State of incorporation.'[60]

The Court came to this conclusion by confirming *Daily Mail* and – in part – *Überseering*, and distinguishing *Cartesio*, on the one hand, from the situations in *Centros*, *Inspire Art*, *Überseering* and *SEVIC*, and on the other hand, from the situation where the transfer of the company seat triggers a change in the national law applicable to the company.

The ECJ started by confirming the *obiter dictum* declared in *Daily Mail*, according to which companies are creatures of national law and exist only by virtue of the national legislation which determines their incorporation and functioning. The premise was restated that the legislation of the Member States varies both concerning the connecting factor required for the incorporation of a company under national law, and with regard to whether this connecting factor subsequently might be modified. Some States require for incorporation that the registered office of the company be situated within their territory while others require that both the real seat and the registered

[59] Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case C-210/06*, p. 131.
[60] *Cartesio*, para. 124.

office be situated in the State of incorporation (Hungary belongs to the latter group of States). Other States permits companies to transfer their central administration to another country (often with restrictions) and the legal consequences of a transfer vary from one Member State to another.[61] There from the Court inferred in *Überseering*, that the question whether a company formed in accordance with the law of a given Member State can transfer its seat to another Member State without losing its genuine legal personality is determined by the national law of the State of incorporation.[62] Consequently, a Member State has the power, first, to define the connecting factor required of a company if it is to be regarded as incorporated under the law of that Member State. In this respect, freedom of establishment does not apply. Secondly, according to the ECJ, the Member State may also prevent a company governed by its law from retaining that status if the company plans to move its seat to another Member State, 'thereby breaking the connecting factor required under the law of incorporation'.[63]

The Court also distinguished the situation in *Cartesio* from the situation where a company moves to another Member State in order to convert into a company form provided under the law of that Member State. In that case, the Member State's power to determine the connecting factor for incorporation and for retaining the status of incorporation 'cannot, […] justify the Member State of incorporation, by requiring the winding-up or liquidation of the company, in preventing that company from converting itself into a company governed by the law of the other Member State, to the extent that it is permitted under that law to do so'. Provisions of the law of the Member State of incorporation that may prevent a company from converting into a company governed by the law of the host Member State amount to a restriction of freedom of establishment which, unless justified by overriding requirements in the public interest, will be prohibited under Article 49 TFEU.[64]

Lastly, the ECJ clarified the scope of *SEVIC*. According to the Court, the situation in *SEVIC* was not concerned with the question of continuing existence of a company under the law of the Member State of incorporation, but whether or not the company is faced with a restriction in the exercise of its right of establishment in another Member State. The situation in *SEVIC* was therefore similar to the situations in *Centros*, *Überseering* and *Inspire Art* and could not be of assistance in a case like *Cartesio*.[65]

The translation of the judgment caused some terminology problems. Whilst the English translation of the reference for a preliminary ruling lodged by the Court of Appeal of Szeged asked the Court to assess the Hungarian laws concerned with the cross-border transfer of the 'registered office' in the light of Community law, the English version of the Opinion delivered by

[61] *Cartesio*, paras. 104-105.
[62] Ibid., para. 107.
[63] Ibid., para. 110.
[64] Ibid., paras. 111-113.
[65] Ibid., paras. 121-123.

AG Poiares Maduro on 22 May 2008 discussed the transfer of Cartesio's 'operational headquarters' to Italy. Meanwhile, both the original Hungarian reference from the Court of Appeal and the Hungarian translation of the AG Opinion used the Hungarian company law term 'székhely' (company seat). In the case of *Cartesio*, neither the registered seat nor the real seat was to be transferred on its own; but what was at stake was rather the transfer of the 'székhely', i.e. the simultaneous transfer of the real seat and the statutory seat. Prior to 1 September 2007 Hungarian law required that these two seats coincided.[66]

Above all, the judgment in *Cartesio* opened new perspectives for the cross-border seat transfer by introducing a fundamental distinction between on the one hand, the cross-border seat transfer of a company with no change as regards the law which governs that company, and, on the other, the transfer with an accompanying change as regards the national law applicable. In the latter situation, the company is converted into a company form governed by the law if the Member State to which the seat is being moved.

## 2.4 New Company Forms

The freedom of establishment in the EU has also taken several steps forward by introducing new supranational company forms. The EU legislator has enacted several regulations in order to create legal forms for business organizations under EU law. The European Economic Interest Grouping (EEIG) was the first to be introduced, and aims at enabling cooperation between entrepreneurs and/or enterprises from different Member States. Almost twenty years later, the European Company (SE) was introduced. The SE is a capital company, and shall facilitate the restructuring of enterprises at a European level. Lastly, the European Cooperative Society (SCE) was adopted as a vehicle for cooperation of natural persons or national cooperative organisations. All these forms are primarily governed by the EU; may transfer their registered seat from one Member State to another and their formation requires a cross-border element. There are, however, frequent referrals to national law which is said to weaken their European character. The European Commission put a proposal for a European Private Company (SPE) forward in 2008.

The introduction of the SE has been hailed as 'a unique and historic step (…) in European law'[67], and will be focused on in the following section and further on in this thesis.

[66] Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case C-210/06*, p. 134 f.
[67] Werlauff, E. *SE – The Law of the European Company*, p. 1.

### 2.4.1 The European Company

The SE was created as a supranational business organisation in order to enable enterprises to restructure their business at Community level. It makes it possible for European businesses to restructure and internationalise. It also offers flexibility, because the SE may transfer its seat across national borders without winding up.[68]

The SE is primarily governed by the SE Regulation[69] itself and, where the regulation expressly authorizes it, its articles of association or statutes. For matters not regulated by the SE Regulation, it is governed by provisions of the law of the Member State in which the SE has its registered office (Article 9).

An SE is a public limited liability company with capital divided into shares. It obtains legal personality upon registration. Primarily, national public limited companies have access to the SE, which, under certain conditions, are even allowed to transform directly into an SE. It is only possible for private limited companies and other legal bodies to participate if they form a holding company or a joint subsidiary respectively.[70]

Formation of an SE may be undertaken according to several methods. These are 'primary' formation methods, in the sense that no pre-existing SE is involved, which is the case concerning the 'secondary' formation methods. Primary formation of an SE can be realized through *merger* between public limited companies, formation of a *holding-SE* by public and/or private limited companies, formation of a *subsidiary SE* by companies and firms within the meaning of Article 48 TFEU or by *conversion into an SE* by a public limited company. The same methods are used when it comes to secondary formation, but the formation is realized with a pre-existing SE (on formation of the SE, see Article 2). There are several provisions in the SE Regulation on the procedure for formation, notably formation by merger and by way of forming a holding company.

The minimum capital requirement is EUR 120,000, and is meant to secure that the SE has sufficient assets without making it too difficult for small and medium-sized undertakings to form SEs. If the law of a Member State requires a greater subscribed capital for domestic companies carrying on certain types of activity, such as financial institutions and insurance companies, the higher amount shall apply to such activities (Article 4).

In regard to employee participation, the separate SE Directive[71] supplementing the SE Regulation is applicable. The starting point can be

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[68] Dorresteijn, A. et al., *European Corporate Law*, p. 103 f.
[69] Council Regulation (EC) No. 2157/2001 of 8 Oct. 2001 on the Statute for a European company (SE), (henceforth the SE Regulation).
[70] Dorresteijn, A. et al., *European Corporate Law*, p. 105.
[71] Council Directive 2001/86/EC of 8 Oct. 2001 supplementing the Statute for a European company with regard to the involvement of employees (henceforth SE Directive).

found in the preamble of the SE Directive, which explains that the creation of an SE simultaneously implies the necessity to introduce information and consultation procedures at a transnational level, as well as the preservation of existing participation rights within the companies establishing the SE.[72] The basis for employee rights of involvement in the established SE should be the employee rights in force before the establishment. As a result, that also applies to structural changes in an existing SE.[73]

The main part of the SE Directive regulates the negotiating procedure. In brief, a special negotiating body is established in accordance with the provisions, in order for the negotiations to commence. The members of this body must be in proportion to the number of employees employed in each Member State by the participating companies and concerned subsidiaries and establishments.[74] The outcome of the negotiations is decided by the negotiating body with an absolute majority of the votes, provided that such majority also represents an absolute majority of the employees. In case the results lead to a reduction of participation rights, a qualified majority is required. If the negotiations fail or if the parties so agree, the Standard Rules, which have to be implemented by each Member States, would apply. These are to be found in the Annex to the SE Directive and include rules for the composition of the body representing the employees, for information and consultation and for participation.

A significant characteristic of the SE is that it may transfer its registered office within the EU without being wound up. This will be further examined under section 3.2.3.

## 2.5 The Cross-Border Mergers Directive

The EU adopted a Directive on Cross-Border Mergers (the Tenth Directive)[75] in 2005, which the Member States should have implemented by 15 December 2007 (Article 19).

The Directive deals with legal mergers which means that there are (1) at least two corporations, (2) a legal transfer of assets and liabilities of at least one of the corporations, (3) the winding up of at least one of them without liquidation, and (4) one remaining corporation (either a newly established corporation or one of the previous corporations).[76] The merger can, however, be realized by acquisition, creation of a new corporation or a merger by transfer of share capital to a holding corporation (Articles 1, 2(2), (a)-(c)).

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[72] Preamble of the SE Directive, Recitals 6 and 7.
[73] Preamble of the SE Directive, Recital 18.
[74] Article 4 of the SE Directive
[75] 10th Council Directive 2005/56/EC of 26 October 2005 on cross-border mergers of limited liability companies ('Cross-Border Mergers Directive' or the 'Directive').
[76] Siems, M. M., *The European Directive on Cross-Border Mergers: An International Model?*, p. 176.

The Directive applies to mergers of limited liability companies formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community, provided that at least two of them are governed by the laws of different Member States (Article 1). It is obvious that the Directive applies to limited liability companies of Article 48 TFEU. Therefore, it is possible for 'letter-box' or pseudo-foreign companies with non-EU origins to participate in cross-border mergers.[77]

In short, the Directive provides for the management of the merging companies to draw up common draft terms of the cross-border merger, which must be published in the national gazette of each of the merging companies. Extra information than for domestic mergers is required with regard to the arrangement for the exercise of the rights of the creditors and minority shareholders (members).[78] The management of the companies also have to draw up a report on the legal and the economic aspects of the merger, which shall be made available to the shareholders (members) and to the employees or their representatives. There is also a requirement for a report from an independent expert. The common draft terms of the merger shall be approved by the general meeting of each of the merging companies.[79] The competent authority must subsequently issue a certificate conclusively attesting to the proper completion of the pre-merger acts and formalities in each of the Member States concerned. Finally, the competent authority of the Member State, where the company resulting from the merger is registered, must scrutinize the legality of the completion of the cross-border merger.[80]

Regarding employee participation, the Directive prescribes that the company resulting from the cross-border merger is subject to the rules for employee participation of the Member State of its registered office. However, these rules shall not apply where they lead to loss of participation rights for all or a certain part of the employees. In that case the issue shall be regulated mutatis mutandis by rules applicable to the formation of an SE. It is not allowed to stage the cross-border merger in such a way as to eliminate pre-existing employee participation.[81]

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[77] Papadopoulos, T., *Legal Perspectives on the Scope of the Tenth Company Law Directive on Cross-Border Mergers*.
[78] Articles 5 & 6 of the Cross-Border Mergers Directive.
[79] Ibid., Articles 7-9
[80] Ibid., Articles 10 & 11
[81] Ibid., Article 16

# 3 Cross-Border Transfers of Company Seats

When one talks about the transfer of a company's seat, it is important to note that there is a distinction made between different types of situations. Firstly, one needs to differentiate between the transfer of the statutory seat (where the company is registered) and the real seat (where the administration and management is situated). Another distinction that needs to be made is between the situation where the transfer of seat is realized with an accompanying change in nationality (and applicable law), and where the company being transferred sustains its nationality. As previously mentioned, the private international law of the Member States as well as their substantive company law determine what the effect of the transfer will be. There are, in other words four different scenarios;

1) the transfer of the statutory seat with a change in nationality
2) the transfer of the statutory seat without a change in nationality
3) the transfer of the real seat with a change in nationality
4) the transfer of the real seat without a change in nationality

What is at issue in the 14th Company Law Directive, and this thesis, is the first situation, i.e. the transfer of the statutory seat (the registered office) with an accompanying change in nationality and applicable law.

## 3.1 Incentives for Transfer of the Registered Office

Why would a company want to take the step of moving its registered seat to another Member State? With today's means of communication, it is possible to handle the operation abroad of many things that a company might want to do. It can appoint foreign agents and sales representatives, set up branches abroad and even incorporate a subsidiary company. The impact assessment mentioned below identifies a number of possible motives underlying a company's decision to move its registered office in the EU. Some could be based on the evidence from non-EU legal systems; in particular, the experience of the United States where the transfer of the company's registered office between the states is possible.[82]

Firstly, differences in company law and corporate governance environment may motivate existing companies to move their registered office, for example reduced capital requirements, less stringent company law with more freedom to define the content of the articles of association, more

[82] Commission Staff Working Document, *Impact Assessment on the Directive on the Cross-border Transfer of Registered Office* (henceforth Impact Assessment), p. 16 f.

choice as to the board structure, different rules on employee participation etc.[83]

A company may also decide to move its registered office to a Member State where company law and insolvency law are considered as more attractive for investors and lenders in order to boost the corporate value of a company, have better access to finance and financial markets etc. [84]

The company may also base its decision to move its registered office because of the generally more efficient judicial system of another Member State, e.g. the speed of rendering judgments, the expertise of judges and legal advisors or more efficient enforcement system. However, these gains would have to be assessed against the costs related to the necessity to litigate in a foreign country. This effect has been shown in Delaware in the US, where e.g. bankruptcy proceedings are considered as efficient. Considering that legal systems of the Member States are more divergent than those of US states, it is likely that the impact of the transfer of the registered office on the share price of a company might be even greater in the EU.[85]

When it comes to tax law, the effect of a transfer of the registered office alone would not result in a change of the applicable law, as the law of the Member State where the 'place of effective management' is situated applies (with some possible exceptions). Similarly, the transfer of the registered office as such would have no impact on employment in the host state, as the labour law is with the country where the company so operating. However, if the company intends to change the registered office and the real seat simultaneously, more favourable tax and labour law may be possible motives.[86]

## 3.2 Existing Alternatives

There are currently a few alternatives to companies that want to move their registered office, with a change in the applicable law, to another Member State, without dissolving the company in the original state and form a new company in the other State.

### 3.2.1 Change of Nationality through National Laws

In several EU Member States, the conflict of law rules prevent companies from deciding where to incorporate because the rules usually require that the company has to be incorporated in the state in which it has its real seat. For

[83] Impact Assessment, p. 16 f.
[84] Ibid., p. 18.
[85] Ibid., p. 19.
[86] Ibid., p. 16.

the same reason, it is not possible for the companies to transfer its registered office to another Member State (see section 2.2.2).[87]

Currently, a corporation can only make an identity-preserving nationality change if there is a legal basis for doing so in the national laws of the Member States concerned or in international agreements. This means that the law of the state of departure allows the corporation to change its nationality without dissolution. If the state of departure allows the corporation to retain its legal personality, it is up to the law of the state of arrival whether the change of nationality can be effected without reincorporation. The Member States differ substantially in the way they deal with an identity-preserving nationality change, both as states of departure and arrival. Only very few Member States' company laws provide for companies registered in their territories to transfer their registered office to another Member State while remaining the same legal person. For example, this is possible under Italian and Portuguese laws, as long as the operation also is possible under the law of the future home state. French law allows a transfer subject to international agreements that do not exist, while German law excludes the possibility outright. The fundamental gap in the company law systems is based partly on the tension between the incorporation theory on the one hand and the real seat theory on the other, as illustrated previously.[88]

### 3.2.2 Cross-Border Merger

The Cross-Border Mergers Directive gives all limited liability companies the possibility to effectuate the transfer of the registered office by means of a cross-border down stream merger. The company first has to set up a subsidiary in the Member State to which it wants to move and then merge the existing company into this subsidiary. This two-step procedure requires that the companies taking part in the merger comply with the provisions of its own national law, particularly those concerning the decision making process.[89]

### 3.2.3 Forming an SE

Another alternative for a company that wants to transfer its seat is by means of an SE. This is, in short, how such a transfer may be realized. First, a Member State (public limited) company converts or transforms itself into an SE (this is only possible, however, if the company for at least two years has had a subsidiary company governed by the law of another Member State).[90] Subsequently, the SE transfers its registered office to another Member State

[87] Sørensen, K. E. and Neville, M., *Corporate Migration in the European Union – An Analysis if the Proposed 14th EC Company Law Directive on the Transfer of the Registered Office of a Company from one Member State to Another with a Change of Applicable Law*, p. 181.
[88] Ibid., p. 191.
[89] Read more about cross-border mergers in section 2.5.
[90] Art 2(4) and Art. 37 SE Regulation.

(Article 8 of the SE Regulation). Finally, then, the SE converts back into a public limited company governed by the law of the Member State in which its registered office is situated. However, no decision on conversion may be taken before, in short, two years have elapsed since its registration (Article 66).

The transfer itself is regulated in Article 8. If effectuated according to the rules of the Regulation, the transfer will neither result in the winding up of the company, nor in the creation of a new company (Article 8 § 1).

As to the formal procedure, it is based on the delivery of a certificate by the home state, stating that the exit formalities have been met (§ 8). The certificate is then produced in the host state, who will inform the home state of the registration in the host state. The company may then be registered in its new home state and the seat transfer will take effect on that date (§ 10). Subsequently, the registration in the former home state will be deleted upon notice sent by the authority of the new state to the authority of the old home state (§ 11). The result of this procedure is change in applicable legislation and change in the articles of association.

The procedure aims at protecting the rights of all the parties that can be affected by the transaction, in other words the shareholders, the creditors and the employees. As § 3 calls for extensive pre-transaction disclosure of the proposal for a transfer, and for the management to report on it, the shareholders receive a chance to take a well-founded decision. The decision has to be taken at least by a 2/3rds majority. Opposing shareholders may be offered appropriate protections according to the law where the SE was registered, e.g. by way of withdrawal right (§ 5). As regards the creditors, the exit certificate cannot be delivered if the SE does not prove that creditors have been adequately protected (§ 7). Furthermore, no transfer is allowed to companies engaged in liquidation, winding up, insolvency proceedings etc. (§ 15). The employees receive insight in the effect of the transfer through the transfer proposal (§ 2 (c)).

Noteworthy is the fact that the SE Regulation requires that both the registered office and the head office of the company be located in the same Member State (Article 7). Thus, it is not possible to transfer the registered office and keep the head office where it was. The sanction for ignoring this requirement and regularise the illegal status of the company is liquidation of the SE (Article 64 § 2).

# 4 The Fourteenth Company Law Directive

In short, the 14th Company Law Directive would make it possible for a company to transfer its registered office to another Member State. The company in question ceases to be a company under the law of the home Member State and becomes a company under the law of the host Member State. During this procedure, legal personality is retained. The assets and liabilities of the company remain belonging to it. If necessary, companies would have to adapt their structures and assets in order to meet the substantive and formal conditions required for registration in the host Member State. However, they would not be obliged to go through liquidation proceedings in their home Member State or to create a new company in the host Member State. The essence of the transfer of the company's registered office would be that the applicable company law changes.[91]

## 4.1 Procedural Background

The search for a workable directive to facilitate cross-border transfer of a company's seat began in 1993 with the publication of a study by the Commission[92], which led to the draft proposal for a Fourteenth Directive on the transfer of the registered office or de facto head office to another Member State with a change in applicable law, issued in 1997.[93]

The issue was also highlighted in public consultations launched by the European Commission in 1997 and 2002. In September 2001, the Commission set up a Group of High Level Company Law Experts with the objective of initiating a discussion on the need for the modernisation of company law in Europe, including the issue of corporate mobility. The report[94] resulted in a recommendation to the Commission to consider adopting a proposal for a Directive on the transfer of a company's seat.

Therefore, the Commission stated in its Action Plan for Modernising Company Law and Enhancing Corporate Governance in the European

[91] See Press Release on 26th February 2004 *Company law: Commission consults on the cross border transfer of companies' registered offices.*
[92] *Study on the transfer of the head office of a company from one member state to another,* KPMG European Business Centre.
[93] Proposal (Com XV/D2/6002/97) of 11 November 1997 for a Fourteenth European Parliament and Council Directive on the Transfer of the Registered Office of a Company from one Member State to another with a Change of Applicable Law.
[94] Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe.

Union[95] that the possibility of corporate mobility would help achieve the overall aim of company law and corporate governance, i.e. to foster efficiency and competitiveness of business. Consequently, the Commission considered a proposal for a Directive on the cross-border transfer of registered office as a means for achieving this. In implementation of this Action Plan, the Commission published an outline of the planned proposal.[96]

In a general consultation, carried out in December 2005, stakeholders were consulted on whether they considered there to be a need for a directive on the transfer of registered office following the recent developments facilitating corporate mobility, *inter alia*, judgments of the Court of Justice on the freedom of establishment and the adoption of the cross-border merger directive.[97]

The consultation showed that a majority of the respondents (79,6 %) thought that there was still a need for a directive on the transfer of registered office, as it would facilitate the mobility of European companies and allow them to locate their business in the Member State that best suits their needs. The stakeholders considered the directive as a means for ensuring legal certainty of the transfer as well as for guaranteeing a proper protection of the interests of creditors, shareholders and employees in relation to the transfer.[98]

Consequently, the Commission stated, in the Commission Legislative and Work Programme 2007, that the Directive on cross-border transfer of the registered office was one of its 'priority initiatives'. All priorities, and thus the Directive are subject to impact assessment.[99] According to the impact assessment, the Commission decided not to submit a proposal for a Directive. The main reasons for abandonment of a proposal for a Directive were, in short, political feasibility, lack of an economic case and the (then) forthcoming *Cartesio* judgment.

The European Parliament, on its end, has stressed the need for a Directive on cross-border transfer of the registered office on several occasions[100], and has adopted a resolution on the issue on 25 October 2007.

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[95] Communication from the Commission to the Council and the European Parliament, *Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward*.

[96] Consultation on an outline for a Directive on transfer of the registered office (2004). See Press Release on 26th February 2004 *Company law: Commission consults on the cross border transfer of companies' registered offices*.

[97] Directorate General for Internal Market and Services, *Consultation on Future Priorities for the Action Plan on Modernising Company Law and Enhancing Corporate Governance in the European Union*, p. 9.

[98] Impact Assessment, p. 7.

[99] Commission Legislative and Work Programme 2007.

[100] European Parliament resolution on the Commission legislative and work programme for 2006; European Parliament resolution on recent developments and prospects in relation to company law.

## 4.2 The Position of the European Commission

The abandonment of the Directive did not come as a great surprise. In June 2007, Charlie McCreevy, the Commissioner for the Internal Market, made the following statement:

> 'But there are also some unresolved issues concerning the cross-border transfer of a company's seat and stakeholders seek more legal certainty in that respect. The Commission had envisaged submitting a proposal for a directive this year.
>
> However, our preparatory work has led me to the conclusion that we should not rush forward with legislation. If we are to propose legislation, we must be sure there is a reasonable chance of a result with added value for business. The economic case is not as obvious or clear-cut as it may seem and Member States currently follow different approaches to which they are strongly attached.
>
> Moreover, the Court of Justice will soon take a decision in a case that could provide us with new insights on the current legal situation in Europe. As you know, the Court has already in the past delivered fundamental judgments in the area of company mobility. I am therefore convinced that we should wait for the outcome of this case which is likely to bring more clarity into this complicated matter. We expect the judgment to be delivered in the autumn of this year.'[101]

Consequently, the adoption of a proposal was put on hold, but was later abandoned altogether. In October 2007, Commissioner McCreevy stated the following:

> '[…] the result of the economic analysis of the possible added value of a directive were inconclusive. Companies already have legal means to effectuate cross-border transfer. Several companies have already transferred their registered office, using the possibilities offered by the European Company Statute. Soon the Cross-Border Mergers Directive, which will enter into force in December, will give all limited liability companies, including SMEs, the option to transfer registered office. They could do so by setting up a subsidiary in the Member State to which they want to move and then merging the existing company into this subsidiary. To my mind it is only if this framework is found wanting, that further legislative action in the shape of a 14th Company Law Directive would be justified. Therefore, I have decided not to proceed with the 14th Company Law Directive.'[102]

When deciding what measure to take, the Commission evaluated different possible policy options. The first option was the *status quo* situation, which means that the current situation remains, i.e. if there were no further developments in the field of company law existing companies wishing to transfer their registered offices to other EU countries would have to establish an SE or SCE and use the transfer option available under these

[101] SPEECH/07/441 of 28 June 2007 (Company law and corporate governance today. 5th European Corporate Governance and Company Law Conference, Berlin).
[102] SPEECH/07/592 of 3 October 2007 (Speech by Commissioner McCreevy at the European Parliament's Legal Affairs Committee, Brussels).

Statutes or, alternatively, wind up a company in the home Member State and re-establish it in the Member State of destination. The second option was *no action*, which would imply no policy change and awaiting the impact of other developments, such as the practical consequences of the cross-border merger directive, the developments of the Community case law or an action on a European Private Company. The third option involved some type of *Community action*. The Commission had to take into account several factors, including applicable law, shareholders' rights, minority shareholders' protection, creditor protection and the employees' involvement rights. The choice of instrument also had to be reviewed.[103]

In a comparison between the *status quo*, the *no action* situation and *Community action*, the Commission found the first (the current situation) to involve substantial burdens in terms of administrative costs, time, financial costs as well as social and tax costs when winding-up and re-incorporating a company. The two latter options were found to provide for less costly solutions. In particular, they ensure the legal continuity of the company and therefore no loss of business and relating costs occur. There is no need for a cumbersome winding-up procedure, but a specific, simpler and less expensive, procedure for cross-border merger or for the transfer. Tax neutrality of the transaction is ensured and safeguards for employees are provided, which, in the current situation, is not legally guaranteed.[104]

Even though the cross-border merger directive would not reduce costs of setting up a new company in the host Member State, these costs were not viewed as substantial in the cross-border transaction. It could also be expected, according to the Commission, that in the future cost differences between the no action option and Community action will be even less significant than they are now. The two options would thus provide for a similar solution to the defined problem. The Commission viewed the no action option as being more proportional seeing as no further EU action is required. It was in its view not clear that adopting a directive would represent the least onerous way of achieving the policy objectives.[105]

## 4.3 The Position of the European Parliament

The European Parliament does not have a genuine right of initiative, which is attributed to the Commission. The Parliament may, however, acting by a majority of it Members, request the Commission to submit any appropriate proposal on matters on which it considers that a Community act is required in order to properly implement the Treaties.[106] The Parliament can also request the responsible Commissioner's presence at the plenary session or in

[103] Impact assessment, p. 29 ff.
[104] Ibid., p. 38 f.
[105] Ibid., p. 38 f.
[106] Art 225 TFEU.

committee.[107] Consequently, the Parliament can put pressure on the Commission, in the case at hand, to adopt a proposal for a Directive on transfer of the registered office.

The European Parliament called on the Commission to submit a proposal for a 14th Company Law Directive in its March 2006 Resolution on restructuring and employment. The Parliament pressed the Commission to submit a proposal under which the transfer of registered office must not be used to restrict workers' rights. The Parliament stressed that the protection of workers' acquired rights regarding their participation in company decisions must be both a fundamental principle and a declared objective of the directive.[108]

A few months later, the Parliament emphasized the need for a Directive in its Resolution on recent developments and prospects in relation to company law of July 2006. The Parliament pointed out that:

> '[…] the transfer of a registered office is today either impossible or hindered by the requirements imposed at national level, that a directive in this area is crucial for freedom of establishment, and that the long –awaited Fourteenth Company Law Directive would fill a lacuna in the system of the internal market for companies; [t]herefore [the European Parliament] calls on the Commission to present in the near future a proposal concerning the Fourteenth Company Law Directive on the cross-border transfer of the registered office of limited companies […]'.[109]

After the abandonment of the Directive by the Commission, in the Resolution on the European Private Company and the Fourteenth Company Law Directive on the transfer of the company seat of October 2007, the European Parliament stated that it:

> '[r]egrets that the Commission, after a considerable delay, has now informed Parliament that it intends to make no legislative proposal for a Fourteenth Company Law Directive on the transfer of the seat,' but '[r]eserves the right, nevertheless, to take further action with regard to the question of cross-border transfers of company seats'.[110]

This statement refers, not only to Article 225 TFEU, but also to Article 265 TFEU, which confers the right on all institutions to bring an action for failure to act against, *inter alia*, the Commission. Thus, the European Parliament showed its intention to keep pressure on the Commission to submit a proposal.

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[107] Pt. 8 of the Interinstitutional Agreement on better law-making of 16 December 2003.
[108] European Parliament resolution of 15 March 2006 on restructuring and employment, pt. 13.
[109] European Parliament resolution on recent developments and prospects in relation to company law, pt. 32-33.
[110] European Parliament resolution on the European Private Company and the 14th Company law directive on the transfer of the company seat.

Consequently, the Parliament adopted a Resolution of 10 March 2009 with recommendations to the Commission on the cross-border transfer of the registered office of a company.[111] It requests the Commission to submit a proposal on the issue,"coordinating Member States' national legislation in order to facilitate cross-border transfer within the Community of the registered office of a company formed in accordance with the legislation of a Member State"[112]

### 4.3.1 Recommendations on the Content of the Proposal Requested

The Annex to the abovementioned resolution contains recommendations on what elements the proposal should comprise. The first recommendation concerns the *effects of a cross-border transfer of the registered office*. The transfer shall not give rise to the winding-up of the company concerned or to any interruption or loss of its legal personality. Thus, the legal identity of the company shall be retained and all its assets, liabilities and contractual relations shall remain unaffected.

The second recommendation deals with the *transfer procedure within the company*. The management or board of a company planning a transfer shall be required to draw up a transfer proposal. The Parliament proposes that there are a few details that should be mandatory to cover, such as the current as well as envisaged legal form, name and registered office of the company, the memorandum and the articles of association of the envisaged company, the timetable for the transfer, the rights guaranteed to the company's members, employees and creditors, etc.

The *shareholders' meeting shall approve the transfer proposal* in accordance with the arrangements laid down and by the majority required to amend the memorandum and articles of association under the legislation applicable to the company in its home Member State, according to the third recommendation. Furthermore, if the company is managed on the basis of employee participation, the transfer can be made conditional on approval on the shareholders' meeting of the arrangements for employee participation.

The question of the *administrative transfer procedure and verification* is found in the fourth recommendation. The home Member State is required to verify the legality of the transfer procedure in accordance with its legislation, and the legality shall be declared in a certificate. This certificate, together with a copy of the memorandum and articles of association envisaged for the company in the host Member State and a copy of the transfer proposal shall be presented to the body responsible for registration in the host Member State. The host Member State shall then give

[111] European Parliament resolution on cross-border transfers of companies' registered offices.
[112] Ibid., pt. 1.

notification of the registration to the home Member State, whereupon the home Member State shall remove the company from the register.

The fifth recommendation concerns *employee participation*, and states that it shall be governed by the legislation of the host Member State. However, this legislation shall not be applicable where it does not provide for at least the same level of participation as operated in the company in the home Member State, or where it does not give employees of establishment of the company situated in other Member States the same entitlement to exercise participation rights as enjoyed by such employees before the transfer. In these cases, the provisions of Article 16 of Directive 2005/56/EC should apply accordingly.

The final fundamental element of the Directive, according to the European Parliament, is that concerning *third parties concerned by the transfer*. Companies shall not be allowed to undertake a cross-border transfer of its registered office if it is involved in proceedings for winding-up, liquidation, insolvency, suspension of payments etc. Furthermore, the company shall be regarded as having its registered office in the home Member State in regard to judicial or administrative proceedings which commenced before the transfer of the registered office.

# 5 Analysis

## 5.1 The Development of Corporate Mobility in the EU

During the past few decades there has happened a great deal in the area of corporate mobility in the EU such as the adoption of new company forms and the Cross-Border Mergers Directive. The SE, for example, is an autonomous European company form which has the possibility of transferring its seat within the EU. The cross-border merger directive makes it possible for companies from different Member States to merge cross-borders, and thereby transfer the company's seat.

However, the continuously evolving case law from the ECJ has proven to catch up with the EU legislator in terms of corporate mobility. In the early *Daily Mail* case the ECJ allowed Member States to place any limit on the transfer abroad of the administrative seat or the registered office of nationally registered companies and, and as a consequence, in identity-preserving company law changes. In other words, it concerns the way the home state is required to treat their companies in line with the freedom of establishment. In contrast, so called 'moving in' cases, such as *Centros*, *Inspire Art* and *Überseering*, concerned limits imposed on companies by the country of arrival. Pursuant to these 'liberal' ECJ decisions, European citizens can incorporate a new company in any Member State even if the company does not operate in the country of incorporation at all, provided that the latter accepts an original divergence between the registered office and the administrative seat. After incorporation, the administrative seat (the real seat) can be transferred to another Member State, which cannot impose unjustified obstacles on this transfer. The ECJ also extended the freedom of establishment to cross-border mergers in the *Sevic* case.

In its most recent judgment, *Cartesio*, the ECJ confirmed the *Daily Mail* judgment in the *Daily Mail* scenario, i.e. that a Member State has the power to determine the connecting factor for a company that wishes to become incorporated under its national law and what is required if the company wants to maintain that status. This includes the power not to allow companies to remain incorporated under their national law when they break the chosen connecting factor. However, the Court also looked at the situation with the outbound transfer of a company's central place of administration with a simultaneous change of the applicable national law. In this case, the company can rely on the freedom of establishment against the Member State in which it has been formed.

The most crucial effect of the decisions in the *Centros*, *Überseering* and *Inspire Art* cases is that founders within the EU are now free to choose the company law they prefer. In particular, companies have been attracted to the

UK, where there *inter alia* is no minimum capital requirements to establish as a private limited company. In order to compete with the more generous company law rules applied in the UK, other Member States, e.g. France, have lowered their minimum capital requirements and now provide simpler formation rules. However, the development of incorporation mobility may have a number of important disadvantages, especially when adopting a foreign corporate law regime. As an example, when a German company employs a UK limited, it might face more costs than initially expected due to the different business environment. These costs may include loss of competitive position, direct compliance costs and administrative costs.

There are mostly smaller start-up firms that are considering the adoption of a foreign corporate law system, as they are more responsive to lower costs rather than the actual corporation law provisions. Some commentators argue that this makes the incorporation mobility resulting from the ECJ case law rather trivial and, because the costs of incorporation is the most important factor in 'choice-of-business-form' decisions, does not provide sufficient incentives for national legislatures to engage in regulatory competition. Correspondently, according to an analysis of the current corporate law reforms in the EU indicates that Member States only respond by reducing the incorporation costs without changing the core elements of their corporation laws or introducing legislative innovations that enable firms to adopt the most effective governance structure.[113]

The *Sevic* case, on the other hand, is viewed as raising the likelihood that medium-sized and large firms may relocate their seat based on the legal rules they prefer. However, it will be difficult to conclude whether the *Sevic* case will lead to an increase in the reincorporation mobility as the implementation of the Directive on cross-border mergers most likely will have a great impact.[114] It is reasonable to assume that the judgment in *Sevic* may reach further than mergers, and that the TFEU also gives a right for a company to realise a cross-border division.[115]

It is too early to determine what impacts the *Cartesio* will result in regarding the EU at large. What is clear is that the problem of the cross-border transfer of the real seat has been resolved for Hungarian incorporated companies. The Hungarian legislator intervened to abolish the restrictions on the seat transfer for Hungarian companies with effect of September 2007, i.e. even before the ECJ delivered its judgment in the *Cartesio* case. The real seat and the statutory seat no longer need to coincide, which means that a Hungarian company has the possibility to move its business activity and the central place of management to any Member State while preserving the statutory

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[113] See e.g. McCahery J.A. and. Vermeulen E.P.M., *Understanding Corporate Mobility in the EU – Towards the Foundations of a European 'Internal Affairs Doctrine'*, A Working Paper Prepared for the 5th European Company Law and Corporate Governance Conference in Berlin on 27-28 June 2007, p. 12.
[114] Ibid., p. 12 f.
[115] Danelius J., *Aktiebolags rörlighet över gränserna*, p. 137. Also see Siems, M.M., SEVIC – *Beyond Cross-Border Mergers*, p. 314.

seat in Hungary. A similar reform has been introduced in Germany.[116] What impact the case might have on the transfer of the registered office and the 14th Company Law Directive will be discussed below.

The fact that the judgments from the ECJ do not contain a clear statement about the different private international laws of the Member States is a main shortcoming of the case law. The ECJ decisions are solely based on arguments relating to the rights provided by the TFEU. Nevertheless, the real seat theory has obviously suffered the most and its effects have been limited.

Despite the *SE's* advantages and possibilities to encourage corporate mobility, the practical usage of it is often questioned. By June 2010, the total number of registered SEs was 596.[117] The reason for this relatively low number might be the minimum capital requirement which is very high in comparison to national public companies. Another reason might be that an SE's head office and registered office are not allowed to be located in different Member States. This is a significant disadvantage, as the management of a company in my view is the most well-grounded when it comes to how the company should be organized.

Although *Sevic* allows for a cross-border merger solely based on the EC Treaty, the Cross-Border Mergers Directive is of guidance e.g. concerning how to deal with creditor protection and the role of employees. The total number of cross-border mergers that have been realised since the adoption of the Directive is not clear, but it is obvious that it has been warmly welcomed not least by legal scholars.

## 5.2 The Economic Case for a Directive

As mentioned above the reason for the European Commission to abandon the 14th Company Law Directive was *inter alia* the lack of an 'economic case'. According to the Commission, companies already have legal means to effectuate a cross-border transfer. The Commission referred to the possibilities offered by the European Company Statute and to a cross-border down stream merger. Commentators have contended that even though the transfer of a company may already be realized, there are important disadvantages to the methods currently available for transfer than a transfer of the registered office under a specific Directive would not have. The transfer of registered office possible for the SE is much too cumbersome and expensive, as it entails transformation into a complicated and intensively regulated legal form. Bearing in mind that re-transformation to a national legal form is possible only after two years, it is particularly viewed as demanding too much of small or medium sized companies. Neither is the

[116] Korom, V. and Metzinger, P., *Freedom of Establishment for Companies: The European Court of Justice confirms and refines its* Daily Mail *Decision in the Cartesio Case C-210/06*, p. 158 f.
[117] According to the ETUI website, http://www.worker-participation.eu/european-company.

resort to the merger possibility satisfactory, also taking into consideration the high costs and roundabout process, especially since a permanent establishment must usually remain in the original state so that hidden reserves are not released. These commentators argue that instead of three separate operations (the SE) or two (down stream merger), a single operation, geared towards transfer of the registered office, would be enough.[118]

The economic benefits of a Directive are, in other words, that the transfer may be realized at lower costs than currently when an SE or a cross-border down stream merger is used. A Directive may also, by the introduction into the law of Member States of a set of similar provisions, ensure that all national legal systems correspond to the requirements of a genuine internal market in which the freedom of establishment is guaranteed. A Directive may also strengthen basic EU principles such as freedom of establishment.[119]

Furthermore, in cases where companies already have moved the main part of their business to another Member States, a transfer of the registered office would probably be an advantage, especially in regard to companies (or nationals) of the host state who consider doing business with the company. In this way, important information costs may be lowered as these companies can rely on simple guarantees that apply when dealing with other companies from their own Member States.[120]

There are, however, some commentators who find the prerequisites for corporate mobility to be relatively satisfactory and that business owners who wishes to move or expand its enterprise cross-borders within the Community have all the means to do so. Consequently, while the Directive may be important from a theoretical point of view, the practical value of the same may be doubted. It has been argued that it would be far more significant if all Member States would accept the incorporation theory as a common European standard.[121]

## 5.3 The Cartesio Case

Apart from the lack of an economic case, one of the reasons the Commission did not submit a proposal for a 14th Company Law Directive was that 'the Court will soon take a decision in a case that could provide us

[118] Vossestein, G-J, *Transfer of the registered office: The European Commission's decision not to submit a proposal for a Directive*, p. 59 f. Also see Speech by Silja Maul at the 5th European Company Law and Corporate Governance Conference in Berlin on 27-28 June 2007.
[119] Ibid., p. 61. Also see The Advisory Group on Corporate Governance and Company Law, Minutes of the 6th meeting of 8 March 2007, d.d. 4 April 2007, p. 4, http://ec.europa.eu/internal_market/company/advisory/index_en.htm
[120] Vossestein, G-J, *Transfer of the registered office: The European Commission's decision not to submit a proposal for a Directive*, p. 61.
[121] See e.g. Danelius, J. Aktiebolags rörlighet över gränserna, p. 140. Also see Pehrson, L., *Kan aktiebolag flytta?*, p. 106.

[the Commission] with new insights on the current legal situation in Europe', i.e. the *Cartesio* case. The case concerned the cross-border transfer of the registered office of a limited partnership from Hungary to Italy, and the company wanted to remain governed by Hungarian law after the transfer. Pursuant to the ECJ's opinion, the TFEU Treaty does not prevent Member States from enacting legislation totally prohibiting a company's emigration if the company intends to continue to be governed by the law of the incorporation state after the cross-border seat transfer. In other words, on the face of it the case does not deal with the same issue that the 14th Company Law Directive would. However, as previously mentioned, the Court also ruled, as an *obiter dictum*, that a Member State may not prevent its 'own' companies from converting into a company which is governed by the law of another Member State (to the extent that it is permitted under that law to do so). Thus, cross-border conversion (i.e. transfer of seat with a change in the nationality of the company and the applicable law) is within the substantive scope of freedom of establishment. What can be noted is that the Court does not distinguish between cross-border conversion into a comparable type of company (e.g. of a private company into (again) a private company) or a different type of company (e.g. of a private company into a public company). Therefore, it has not been excluded that even this second form of conversion is within the scope of the freedom of establishment.[122]

It is important to note that, according to the judgment, Article 49 compels the Member State of incorporation *to recognize* the possibility of a conversion under the law of another Member State, but that the Court does not explicitly rule on an obligation for the Member State of relocation. The Member State may, however, not refuse generally that the status of company under its law is obtained.

The question is whether the *obiter dictum* in *Cartesio* reduces or removes the need for a 14th Company Law Directive. Some argue that, in view of the outcome of *Cartesio*, there is an even more urgent need for such a Directive. Although the judgment has direct effect and individuals may invoke Article 49 both against Community and national authorities, a Directive may be a more effective means of eliminating the restrictions concerned as case law always concerns individual cases resulting from specific circumstances and measures in a particular Member State. A judgment in an individual case cannot replace transparent substantive and procedural rules regarding the cross-border operation or remove obstacles resulting from different approaches to conflict of law problems. An example of a problem that has not (and could not) have been resolved by the ECJ judgment, and that needs to be dealt with in secondary legislation, is employee participation.[123]

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[122] See Vossestein, G-J, *Cross-Border Transfer of Seat and Conversion of Companies under the EC Treaty Provisions on Freedom of Establishment*, p. 120.

[123] Vossestein, G-J, *Cross-Border Transfer of Seat and Conversion of Companies under the EC Treaty Provisions on Freedom of Establishment*, p.123. Also see Wisniewski A. and Opalski A., *Companies' Freedom of Establishment after the ECJ* Cartesio *Judgment*, p. 620 f.

Without a Directive, a company's entitlement to the exercise of the freedom of establishment in the form of conversion depends on the choices made autonomously by the national legislators. Currently, the national company laws generally lack any regulation permitting international conversion (i.e. transfer with a change of the applicable law). Many commentators have drawn the conclusion that the European legislator really has no other choice but to provide adequate regulating mechanisms.[124]

[124] See e.g. Wisniewski A. and Opalski A., *Companies' Freedom of Establishment after the ECJ* Cartesio *Judgment*, p. 621.

# 6 Conclusion

This thesis has shown that much has been done in the field of corporate mobility, but that the possibility of a transfer of the registered office with a simultaneous change in applicable law has not yet been clearly provided. On the basis of the analysis, it is in my view obvious that an adoption of a 14th Company Law Directive is indispensable.

In spite of the existence of alternative methods for a transfer of registered office, they are not satisfactory as the disadvantages of them override the advantages. A transfer by way of an SE or a cross-border merger seems like a much more cumbersome and costly method in comparison to an immediate transfer regulated by a Directive. The SE is not suitable for all companies, as it requires a large amount of capital to be created. In addition, the SE needs to wait two years until it can be transformed into a national company form in the new Member State. Since the head office and the registered office are required to be located in the same Member State, the SE does not offer a flexible enough alternative.

The long awaited *Cartesio* case was hoped to bring clarity to the issue. Though it was gladdening that the ECJ in an *obiter dictum* assessed the transfer of the registered office of a company with a change in nationality and applicable law to be within the scope of the freedom of establishment provided by the TFEU, it is in my view not an adequate basis for a company who wishes to transfer its registered office. I believe it is a question of legal certainty, which an individual case simply cannot offer. It is not only because the case deals with a particular situation, but also because a judgment will never be able to provide for the detailed rules that a Directive will. Many questions need to be dealt with, such as employee participation and tax issues not to mention the way in which the transfer will be effectuated in practice. Another important issue that needs to be regulated is that concerning shareholder and minority protection. If a Directive would be on the carpet in the future, I deem it as essential that these questions are regulated and that as few as possible of them is referred to national law to determine, in contrast to the SE Regulation. If not, a harmonisation would be to no purpose.

The need for a 14th Company Law Directive is not least of principal significance. If the intention of the EU is to create one single market, why not do it to the full? If a Member State wants to retain its companies within the territory it can modify its company laws. This will lead to more competition between the Member States, creating a beneficial environment for companies. Additionally, the competitiveness of EU companies will be enhanced on an international level. Accordingly, a proposal for a 14th Company Law Directive is to be desired and I look forward to seeing the course of events in the near future.

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