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***Cross-Border Transfer of Registered Office
Moving Beyond Forms***

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Summary

The Court decision in *Daily Mail* has come as a result of the resolution of the Member States to endorse a plurality of national legal solutions in the field of tax and corporate laws. The free movement provisions must be understood against this background and keeping in mind that no matter which “*interface program*” is to be used the system as a whole, i.e. the internal market, must be effective and coherent. The term “*interface program*” is used here as a metaphoric representation for the set of rules enshrined in national tax and corporate legislation that stipulate conditions for the entry and exit of companies.

Among the exit conditions, the liquidation or winding-up of companies as a prerequisite for the cross-border transfer is the most radical one. It’s the main pursuit of this study to scrutinize the legality of liquidation in relation to cross-border movement of companies, operation which presupposes a change of the applicable law.

Once a company is lawfully established in the State of origin and its transformation into a company governed by a different national corporate law is allowed by the State of destination, the movement represents a matter falling within the scope the Article 49 TFEU. Implicitly any restrictions imposed on the movement will be subject to the Treaty provisions.

The present study makes the distinction between the conditions imposed by the State of destination, which concern rules on company transformations under the national laws and the ones imposed by the State of origin on an emigrating company. The first set of conditions falls within the State competence to determine the formal requirements necessary for the acquirement of legal status under the domestic laws, while the second set of conditions can only be applied in order to preserve the protection of rights originating before the transfer.

The liquidation belongs to the latter set of conditions and according to the findings of this study, even if it is not generally excluded, the application of such restriction in a specific case would be rarely, if ever, found to be proportionate and its lack of proportionality will render it illegal under the Union law.

Preface

The present dissertation marks the closing stage of my postgraduate studies in European Business Law and the beginning of a new phase in my life. Hence I would like to address most sincere thanks to my study counsellors, professors and dear colleagues for the fantastic memories that I will henceforth bear in my heart.

G.K. Chesterton asserted once that thankfulness is the highest form of thought, and that gratitude is happiness doubled by wonder. I feel equally happy and grateful for the auspicious opportunities, which have enabled me to meet a truly remarkable personality and accomplish a series of assignments under his supervision. Thank you, Professor Xavier Groussot for two absolutely wonderful years!

The source of inspiration for this study is likewise not a usual one; it relies partly on the facts of a fictive case, which is the creation of a resourceful mind. In view of that, my final thanks are addressed to René Repassi, Professor at the Heidelberg University and author of the ELMC Competition case this year. I have greatly enjoyed working with this subject and I hope that the present study can be of definite benefit to its addressees.

Abbreviations

AG	<i>Advocate General</i>
CBM	<i>Cross-Border Mergers</i>
ELMC	<i>European Law Moot Court</i>
EU	<i>European Union</i>
IPO	<i>Initial Public Offer</i>
IRS	<i>Internal Revenue Service</i>
NASDAQ	<i>National Association of Securities Dealers Automatic Quotations</i>
PIL	<i>Private International Law</i>
SCE	<i>Societas Cooperativa Europaea</i>
SE	<i>Societas Europaea</i>
SME	<i>Small and medium enterprise</i>
SPE	<i>Societas Privata Europaea</i>
TEU	<i>Treaty on the European Union</i>
TFEU	<i>Treaty on the Functioning of the European Union</i>

1. Introduction

1.1. Background

Companies exist only by virtue of the varying national laws determining their incorporation and functioning.¹ I would add also that companies cease to exist by virtue of national legislation, thus the *birth* and the *death* of a legal person have a predominantly formal character. The act precedes the fact because the company starts or ceases to exist after the relevant formalities have been completed. On the contrary, concerning natural persons the relevant formalities attest the fact of coming into existence or ceasing to exist. For this reason the formalities related to formation and dissolution of companies play an essential role and their impact on the free movement of companies is cardinal.

Dissolution without liquidation is preferred by the company shareholders for tax reasons. Company liquidation entails the conveyance of the net assets towards the shareholders. This transaction has the character of a net distribution and the afferent capital gain will be taxed accordingly and often immediately by the State of origin.

The State of origin retains, in conformity with Union law, the power to define both the criteria for allocating their powers of taxation and the corporate nexus required of a company in order to obtain or maintain its legal status under national law.² It would be absurd according to AG Darmon if a Member State not requiring liquidation were to find itself placed by Union law in a less favourable fiscal position just because its legislation on companies is more compatible with Union objectives in regard to establishment.³

¹ Case 81/87 Daily Mail para 19

² Case C-371/10 Grid Indus

³ Case 81/87 Daily Mail AG Darmon point 13; See also Opinion of AG Kokott in Grid Indus point 29

Treaty rules on freedom of establishment apply nevertheless to national legislation on the incorporation and liquidation of companies.⁴ An automatic ban interfering with the very essence of the right to move and to be established in another Member State is precluded by Union law and in any case the proportionality principle must apply in law and in practice on any type of absolute prohibition.⁵

AG Jääskinen expressed the opinion that the rules on transfer of registered office applicable on supranational forms of corporation could shed light on the cross-border transfer of companies formed under national laws. According to these rules the legal succession is possible only if the successor exists before the predecessor has lost its legal capacity.⁶ In the aftermath of *Daily Mail* and *Cartesio*, it seems nevertheless plausible that the national legislation imposing the liquidation of a “*creature of national law*” is not precluded by the Union law in the event of a cross-border transfer of social seat.

Following AG Tizzano’s insightful observation in *SEVIC Systems*, I have distinguished in this paper between the different phases of a company transformation and tried to highlight the source and the nature of the conditions and preconditions that might be imposed on a migrating company. In this way, I try to explain how the ostensible contradiction between *Daily Mail* and *SEVIC Systems* can be elucidated.

⁴ Case C-371/10 *Grid Indus* para 30

⁵ Compare *Riener v Bulgaria* and *I.M. v France* with Case C-408/03 *Commission v Belgium* para 68 and cases C-402/05 P and C-415/05 P *Kadi* para 355

⁶ Point 52 of the Opinion in *Vale* : En revanche, la continuité de l’existence juridique de la première société au moment de la naissance juridique de la société destinée à lui succéder en droit revêt un autre aspect tenant aux conditions fixées par l’État membre d’accueil afin que la société en formation puisse être considérée comme le successeur de la première société. La législation italienne ainsi que les dispositions analogues du droit de l’Union partent du principe selon lequel la succession n’est possible que si le successeur existe avant que le prédécesseur ne perde sa capacité juridique. See also Article 8 of the SE Regulation.

1.2. Topic

Dissolution with liquidation is often the practical solution adopted by the companies or more accurately that the companies are compelled to adopt. It is reasonable to inquire whether or not the exercise of the right to free movement of companies is completely deprived of its substance in this case. Liquidation means after all that the company ceases to exist as a legal person. The company formed afterwards in another Member State is a new legal person and according to the reasoning of AG Jääskinen in *VALE*, this person cannot be recognized as the legal successor of the dissolved company.

The article 54 TFEU prescribes that within the scope of freedom of establishment, 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 Union shall be treated in the same way as natural persons who are nationals of Member States. Is the equality before the law of legal and natural persons observed in practice?

According to AG Jääskinen if the dissolved company wasn't allowed to maintain its legal personality, the universal transfer of assets wouldn't be possible at all. The reason is simple; a transfer presupposes an operation between two companies. If the dissolved company has lost its legal status at the time of the new registration, the only possible predecessor would be either a partnership without legal personality or the associates seen either as individuals or as a collective.⁷ An interesting question is whether or not the freedom of capital could apply in the latter case.

1.3. Purpose

The aim of the paper is to scrutinize the legality under Union law of the liquidation as restrictive condition imposed on companies that envisage a cross-border movement. In order to fulfil this quest I will pursue to answer a series of supporting questions.

⁷ Conclusions de l'avocat général Jääskinen présentées le 15 décembre 2011 dans l'affaire C-378/10 point 79

Are there any situations of possible abuse of law or the transfer or conversion in itself constitute a genuine economic activity? If the exercise is genuine which economic freedom would apply? Can we still discuss about the free movement of companies in the case of dissolution with liquidation? Does the equal treatment of legal and natural persons as expressed in the Article 54 TFEU have any practical relevance? Should liquidation be regarded as an absolute ban or as a preliminary requirement?

1.4. Delimitations

National company law is enacted as known by Member States. This paper does not contain a comparative study of the company laws of different Member States and the references to the national legislation in this context are merely acquired from the case law of the Court and ordinary principles applicable to company law. More exactly I use these common principles as a benchmarking; rules that deviate from the benchmarking constitute potential restrictions by either denying adequate protection or affording overprotection to some of the interested parties.

1.5. Method and Material

The first question that I will pose is whether or not the cross-border transfer of social seat or conversion serves in itself a genuine economic pursuit. If not I will determine which are the conditions to fulfil in order to fall under the scope of the economic freedoms. Article 54 TFEU aims to ensure the equal treatment of natural and legal persons for the scope of Article 49 TFEU, while the decisions in *Daily Mail* and *Cartesio* seem not to respect this prerequisite. I will analyze these decisions in the light of the recent case law and provide an explanation to the outcome of the above named cases.

Union secondary law provides several legal vehicles for company movement: cross-border mergers and certain supranational forms of legal entities. All these legal instruments envisage the solution of transfer or conversion without liquidation. Therefore I will compare the conditions required by the secondary law with the conditions implied from the case law on companies' movement.

Against this background, I will attempt to analyze the nature of liquidation as precondition for transfer. If the analysis may lead to the conclusion that Article 49 TFEU does not preclude liquidation as a condition for transfer I will continue the analysis under Article 63 TFEU and briefly inform on the possibility to oppose the restriction under this freedom. I will conclude by giving my opinion on the nature of liquidation in the context of free movement of companies.

1.6. Outline

The first chapter contains the introduction, which as expected sets up the main concerns of this study, the purpose and the methodology to be used further on in the present paper. The second chapter gives an account of the legal definitions of the economic freedoms as established by the relevant case law. The subchapter on the free movement of capital gives a factual example from the contemporary reality: the Facebook IPO and the tax planning scheme used by one of the company founders. The third chapter takes a deeper view of the possible exit restrictions and discusses whether their nature is merely formal or not. The fourth chapter examines the acts of secondary legislation concerned with forms of supranational association, mergers and transfer of social seats. The fifth chapter investigates the issue of abuse of law in relation with cross-border movements of companies and the sixth chapter concludes the present study by construing the set of rules previously evoked and giving a confluent perspective of their joint points. The areas of confluence can provide valuable explanations concerning the nature of liquidation as a precondition for a cross-border movement.

2. Economic Freedoms and Exit Rights

2.1. The Concept of Establishment

The concept of establishment is far-reaching allowing Union nationals to participate, on a stable and continuous basis, in the economic life of a Member State other than his State of origin and to profit there from, so contributing to economic and social interpenetration within the European Union in the sphere of activities as self-employed persons.⁸ The maintenance of a permanent presence in the State of Destination by an undertaking established in another Member State may fall within the provisions of the Treaty on the freedom of establishment, even if that presence does not take the form of a branch or agency, but consists merely of an office managed by a person who is independent but authorised to act on a permanent basis for that undertaking, as would be the case with an agency.⁹

Cross-border establishment comprises the right to entry and maintain a permanent presence on the market of another Member State under the same conditions as the nationals of that other Member State. According to case law, the form chosen in order to exercise the right of cross-border establishment i.e. primary/secondary establishment, merger & acquisitions, conversion or transfer of social office does not change the substance of the right. These methods of exercise of freedom of establishment fall under the scope of the Article 49 TFEU, with only one exception, which is the case of transferring the corporate nexus with no subsequent change of the applicable law.¹⁰

The mobility of companies within the EU, in terms of either transferring the social seat or setting up new companies or secondary establishments of existing companies, is the result of creation and functioning of the internal market, i.e. an area without internal frontiers in which free movement of persons must be preserved.¹¹

⁸ Case C-55/94 Gebhard para 25; Case C-97/09 Schmelz, para 37

⁹ Case C-409/06 Winner Wetten, para 46

¹⁰ Case C-411/03 Sevic Systems, paras 18-19

¹¹ Articles 3(3) TEU and 26(2) TFEU

2.1.1. Company transformations in SEVIC Systems

Member States had to bring into force the laws, regulations and administrative provisions necessary to comply with the Merger Directive before the 15th of December 2007. The *SEVIC Systems* case has been decided two years prior to this transposition deadline. It concerns a German company which was prevented to merge a Luxembourg one, because the German law didn't contain any provisions for the registration of a merger between a German and a non-German company. Company transformations, including mergers, mean to fulfil the needs for cooperation and consolidation between companies established in different Member States.

The Court established that company transformations constitute particular methods of exercise of the freedom of establishment. They are central for the proper functioning of the internal market and as a result, they constitute economic activities in respect of which Member States are required to comply with the freedom of establishment laid down by Article 49 TFEU.¹²

I must underline also that it is a German company that brings before a German Court the issue of its right of establishment in a different Member State through a merger with a local company. AG Tizzano explains that it's important to distinguish between the pre-merger phase, when both companies have legal personality, and the post-merger phase, when we deal with only one legal entity having German personality. Preventing a company established under the national to participate in cross-border transformations constitutes a serious impediment against the free movement of capital¹³ and the freedom of establishment¹⁴. A general refusal to register embodies an absolute form of prohibition comprising all cross-borders transformations.

¹² Case C-411/03, *SEVIC Systems* paras 18-19

¹³Case C-222/97 *Trummer and Mayer*, para 24; See also AG Tizzano in Case C-411/03 *Sevic Systems*, point 76

¹⁴ Case C-411/03, *SEVIC Systems*, para 31

2.2. Cartesio judgment

2.2.1. Home Country Restriction- Transfer of Central administration

Cartesio was a Hungarian private limited liability company with registered office and central administration located in the South of Hungary. On the 11 November 2005 it applied for a change in the Hungarian company register mentioning the transfer of central administration to Gallarate in Italy. The application has been rejected on the ground that the transfer was not possible as long as the company remains subject to Hungarian law.

The applicant contested the refusal of the Hungarian Company Register and the case was finally brought before the Court of Appeal of Szeged that decided to stay the proceedings and refer the questions to the Court of Justice of the European Union for a preliminary ruling assessment. AG Maduro determined in his Opinion that Hungarian law discriminated between within- and cross-border transfers of central administration and found a restriction of the free movement of companies.

By referring to the judgments in *Centros*, *Überseering*, *Sevic* and *Inspire Art*, AG Maduro asserted that any kind of cross-border movements of companies shall be included within the scope of Article 49 TFEU as long as the conditions stipulated in Article 54 TFEU are satisfied. As known the Court did not confirm the AG Opinion and followed instead a line of reasoning closer related to *Daily Mail*.

Even if the Court ruled in favour of the defendant in *Cartesio*, it has used the opportunity given by this reference for preliminary ruling in order to clarify that a situation of transfer with change of applicable law must be distinguished from a situation of transfer without such a change. In the second case it is up to the State of destination to determine the conditions for registration.¹⁵

¹⁵ Case C-210/06 CARTESIO Oktató és Szolgáltató, para 111

If *Cartesio* is to be placed within a larger picture, the State of origin may also impose other type of conditions, which in case they satisfy the requirements entailed by free movement provisions would not be precluded by Union law. The best example in this sense is provided by the decision of the Court in *National Grid-Indus*, according to which exit taxation will be considered lawful under Union law as long as the fiscal burden is proportionate and does not rely on a presumption of abuse.¹⁶ On the other hand, preventing a company from converting itself into a company governed by the law of the other Member by requiring the winding-up or liquidation of the company is precluded by Article 49 TFEU whereas the laws of the State of destination permit the conversion.¹⁷

2.2.2. Cartesio- From a PIL perspective

Even if the Court has avoided analysing the *Cartesio* line of cases from a private international law perspective, namely the formation of a company in international company law, this implied aspect is not irrelevant. All the three locations mentioned in Article 54 TFEU, central administration, registered office and principal place of business, constitute connecting factors in private international law. By choosing to transfer its registered office to a different Member State, a company may also opt for a new corporate nexus concerning jurisdiction of courts in company law matters.¹⁸

¹⁶ See also Case C-264/96 ICI, para 26; Case C-478/98 Commission v Belgium, para 45; Case C-436/00 X and Y, para 62; Case C-334/02 Commission v France, para 27; and Case C-196/04 Cadbury Schweppes and Cadbury Schweppes Overseas, para 50

¹⁷ Case C-210/06 CARTESIO Oktató és Szolgáltató paras 112-113

¹⁸ Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, Articles 22(2) (exclusive jurisdiction) in conjunction with Article 60.

Although there is no regulation under Union law concerning the uniform conflict of law rules in company law matters¹⁹, the possibility to opt for a new forum through a change of the corporate nexus plays always an important role for the outcome of an impending judicial trial. An expected change of the tax residence through a transfer of social seat might in fact have other purposes than a more favourable tax regime.

By omitting to analyse the private international law aspect, one of the often less visible reasons, especially from a third party's perspective, might be ignored. I use this context in order to underline that a change of the social seat is a decision that always must consider a complex set of causes and expected consequences, whereas more favourable tax rules constitute only one of the critical factors.

2.3. Case law post-Cartesio

2.3.1. National Grid Indus - Transfer of Central Administration

The case is about a Dutch company, National Grid Indus that relocated its place of central administration from the Netherlands to the UK. National Grid Indus held a sterling denominated receivable on a UK group company which borne out an unrealized foreign exchange gain at the time of the transfer. According to the tax treaty concluded between the Netherlands and the UK, National Grid Indus's tax residence was changed to the UK after relocation, with the result that its profits, including any unrealized gains, were only taxable in the UK. The change of central administration triggered a Dutch exit tax liability.

¹⁹ According to Article 1(2) f of the Rome I Regulation, the matter falls outside the scope of the Regulation on uniform conflict of law rules applicable to contractual obligations. See also Article 1(2) d of the Rome II Regulation.

First at all there is no change of applicable law in this case. National Grid Indus continues to exist as a Dutch company. A transfer of place of central administration within the borders can be compared with a cross border one. Only the latter triggered exit taxation and therefore it has been considered to imply a restriction of the freedom of establishment. The operation of transfer of central administration falls within the scope of the freedom of establishment.

The conclusion is that even if the relocation of the place of central administration could in specific situations entail circumvention of taxes, this fact alone cannot be invoked by the State of origin in order to justify a restriction on free movement. Following this decision of the Court, the Netherlands has to change its exit tax rules and offer taxpayers the option between immediate taxation and deferral, whereby in any event it has no obligation to consider a subsequent value depreciation of the assets subject to exit taxation.

The power of the Member States to define the corporate nexus within the scope of their domestic company law does not mean that the Treaty rules on freedom of establishment do not apply to national legislation on the incorporation and winding up of companies. The *Cartesio* dictum has been recently confirmed in *National Grid Indus*.²⁰

2.3.2. VALE- Host Country Restriction- New establishment

The case is about an Italian company, VALE Costruzioni Srl which intended to be converted into a Hungarian company. Company conversion was a procedure known in Hungary for domestic companies but not applicable in a cross border situation. On 3 February 2006, the company demanded to be removed from the Italian Company Register with the note that it intended to transfer its seat and activities to Hungary. On 13 February 2006, the removal has been registered.

²⁰ Case C-371/10 *National Grid Indus* para 30 referring to para 112 in Case C-210/06 *CARTESIO* Oktató és Szolgáltató

Nine months later a Hungarian private limited liability company, VALE Építési kft was established by one of the directors of VALE Costruzioni Srl. A representative of the new company sought to have it registered by including mention of the fact that VALE Costruzioni was the legal predecessor of the new formed company and all rights and obligations of the Italian VALE should be transferred to the Hungarian VALE. The intention was to achieve a cross-border company conversion. This procedure was available under domestic law, but a specific provision allowing for such a reference to a foreign legal predecessor didn't exist. Thus the application was rejected.

Eventually the legal proceedings reached the Hungarian Supreme Court and a reference for preliminary ruling has been made. Was VALE Építési kft allowed to have VALE Costruzioni Srl as its legal predecessor or in other words must Hungarian law allow a cross-border company conversion?

It is easy to observe the discordance between the intention of the Italian companies' representatives and the actual result of the cross-border operation. Even if the intention was to convert the actual result is that a new company has been established under Hungarian law. The factual situation of *VALE* is one similar with a merger between the initial Italian company and the new established Hungarian company.

The Judgment in *VALE* will probably be delivered after the summer judicial vacation. The element of continuity of legal personality is not present in this case since the actual cross-border conversion was not approved by the laws of the State of destination. According to the opinion of AG Jääskinen, these laws shall permit a company to publish its status as a successor of another company, implying that the company being formed takes over all the rights and obligations of its successor.²¹

²¹ C-378/10 VALE Opinion of AG Jääskinen point 78

2.4. The concept of free movement of capital

The free movement of capital and freedom of establishment overlap in particular where national legislation concerns direct forms of investment.²² The existence of Article 65(2) TFEU and the expression “*subject to the provisions of the chapter relating to capital*” contained in Article 49(2) TFEU seem to suggest that in such cases neither the one nor the other fundamental freedom is rejected, but that both fundamental freedoms can be applied alongside each other.

According to the decisions of the Court in *National Grid Indus* and *Cartesio*, the national legislation imposing a preliminary condition of liquidation on the migrating company does not fall outside the scope of the freedom of establishment. This restriction relates to a preliminary phase, a stage prior to the time point when the company may actually move.

In this first phase, we deal according to the AG Tizzano in *SEVIC Systems* also with a planned movement of capital towards the State of destination. A separate assessment under the Article 63(1) TFEU would not be however necessary since all the considerations expressed in relation to the Article 49 TFEU will apply *mutatis mutandis*. The rules in question have at the very least a dissuasive effect on capital movements as they disallow the use of an advantageous vehicle for carrying out company transformations abroad.²³

Article 65(2) TFEU guarantees that both fundamental freedoms are subject to the same restrictions.²⁴ This provision aims to deny the possibility of third country nationals to claim the illegality of a restriction against the free movement of capital, where this restriction would not fall within the scope of Article 49 TFEU in the first place.

²² Opinion of AG Stix-Hackl *Centro di Musicologia* Case C-386/04 point 37

²³ Opinion of AG Tizzano Case C-411/03, *SEVIC Systems* points 76-77

²⁴ Opinion of AG Kokott in Case C-265/04 *Bouanich* point 71

In *Commission v France* Case C-483/99 the defendant counterclaimed that golden share rules applied without distinction between nationals and non-nationals. The Court rejected this counterclaim by establishing that the general prohibition in Article 63 TFEU goes beyond the mere elimination of unequal treatment.²⁵ *Dassonville* formula applies on the free movement of capital.²⁶

Dissolution with liquidation implies firstly a divesture in the State of origin followed by the re-integration of the assets under the law of the State of destination. A physical transfer of assets is not necessarily succeeding this formal transformation. The accounts of the liquidated company are closed and an initial balance sheet is created for the new-formed company. The wealth of the shareholders is reduced proportionally with the fiscal and administrative burden afferent to the transfer.

The core of the concept of limited liability relies on the idea that shareholders and the company in which they have invested capital are separated entities. This paper is concerned with the legal person, the company as right holder. On the other hand, it is important to envisage the whole picture in a chronological sequence. The existence of a company starts with the act of direct investment, by which the shareholders exercise rights related to both capital movement and establishment. In *VALE* the shareholders exercised as well the right to be re-established abroad, which involves a simultaneous cross-border transfer of capital.

Only if the company ceases to exist and the assets are conveyed to the shareholders, the question concerning the economic freedoms conferred by the Treaties on the shareholders becomes prevalent. On the other hand if the company's legal personality is not discontinued at the time of the cross-border transfer no analysis of the free movement of capital would be necessary.

²⁵ Case C-483/99, *Commission v France*, para 40

²⁶ Case 8-74, *Procureur du Roi v Benoît and Gustave Dassonville*, para 5 confirmed by Case C-222/97, *Trummer and Meyer*, para 26

2.4.1. Permission to exit?

It is recognised that the measures prohibited by Article 63(1) TFEU as restrictions on the free movement of capital, include those which are likely to discourage non-residents from making investments in a Member State or to discourage that Member State's residents from doing so in other States.²⁷

In *Verkooijen* case the Court established that granting an exemption from income tax payable on dividends paid to natural persons, as shareholders, subject to the condition that those dividends were paid by a company whose seat was in Netherlands constituted a restriction on the companies established in other Member States. In comparison with the shares in companies which had their seat in Netherlands, the shares of the companies established in other Member States were made less attractive to investors residing in the Netherlands.²⁸

According to AG Léger the mere transfer of tax residence does not constitute in itself a movement of capital.²⁹ The change of tax residence alone does not have any influence on the composition of assets and location of accounts and does not imply a transfer of ownership title. On the other hand an exit tax has in itself the effect of reducing the value of the assets concerned and according to the decision of the Court in *Barbier* it impedes the movement of capital.³⁰

²⁷ Case C-513/03 *van Hilten-van der Heijden* para 44; Case C-370/05 *Festersen* para 24; and Case C-101/05 *Skatteverket v A* para 40

²⁸ Case C-35/98 *Verkooijen* paras 34-35; See also Case C-446/04 *FII Group Litigation* para 64; Case C-310/09 *Accor* para 69

²⁹ Case C-513/03 *Opinion of AG Léger van Hilten-van der Heijden* point 68

³⁰ Case C-364/01 *Barbier* paras 62-63; See also Case C-450/09 *Schröder* (anticipated succession inter vivos) paras 32-33.

It is important to remind that due to the allocation of taxation powers between Member States, the tax neutrality of the transfer is not guaranteed by Union law.³¹ Certain Member States impose an exit tax on a migrating company, if the latter ceases to be a tax resident as a result of the transfer according to domestic tax rules. Exit taxation is also imposed on migrating companies that cease to exist under the company law of the Member State of origin, i.e. dissolved companies.³²

It is obvious that an exit tax can be liable to render the transfer less attractive or very difficult, all depending on the conditions of tax imposition and payment. Tax measures in a Member State which dissuade taxpayers in that State from investing their capital in companies established in other countries, including third countries, are prohibited by Union law, unless they are justified and proportional.

2.4.2. The ultimate plan: Citizenship renunciation

In this subchapter I will provide an example of international tax planning in relation to the question of taxation of unrealized capital gains and change of tax residence from U.S. towards Singapore. Since the facts are related to the well-known public company, Facebook, I find this example to be useful for the understanding of the decisional premises that generally must be considered at the time of the transfer.

³¹ Case C-336/96 Gilly, para 47 Hence, even the transfer of residence does not have to be tax neutral (see Case C-387/01 Weigel, para 55; Case C-365/02 Lindfors, para 34; and Case C-67/08 Block, para 35)

³² The taxing rights are connected to: Hidden reserves (profit realized but not yet taken into account) & provisions (expenses already deducted but not yet incurred) and unrealized capital gains (the positive difference between fair market value and the tax value).

U.S. nationals who renounce their citizenship are obliged to pay an exit tax on the capital gains from their stock holdings, even though they don't sell any shares. One of the three original founders of Facebook, Eduardo Saverin, who holds 4% of the Facebook stock, renounced his U.S. citizenship on the 30th of April this year, less than three weeks before the initial public offer has been launched. Once Facebook goes public, its stock will be listed and sold on the NASDAQ.³³

The estimated value calculated by the American Tax Office (IRS) for fiscal purposes at the time of transferring the tax residence from the U.S. to Singapore is expected to be lower than the market value of the stock, since the IPO has already been oversubscribed.³⁴ The difference between these two values generates an amount of tax being avoided by the shareholder. The transfer of tax residence does not incur any change in the composition of the assets; no transfer of capital takes place.

The change of tax residence through citizenship renunciation can be seen as being formal in nature. The change of form has nevertheless financial consequences within a predictable future and there is an economic rationale that takes into account several aspects besides the obvious reduction of the upcoming tax debts. The financial analysts on the Stock Exchange have already expressed the opinion that Facebook stock was overrated.³⁵ This means the difference between the fiscal value at the moment of transfer and the corresponding market value after the transfer is uncertain and the decision of citizenship renunciation implies a genuine financial risk.

³³ Facebook plans to price its Initial Public Offer (IPO) on May 17, offering 337.4 million shares at \$28 to \$35 each. By Danielle Kucera, Sanat Vallikappen and Christine Harper - May 12, 2012 12:58 AM GMT+0200 on Bloomberg

³⁴ Alexei Oreskovic and Olivia Oran, <http://www.reuters.com/> Friday May 11, 2012 8:53 EDT

³⁵ Tom McCarthy, guardian.co.uk, Tuesday 22 May 2012 21.16 BST

As one can observe in Saverin's case, he is Brazilian-born, who lives now-a-days in Singapore and became U.S. citizen fourteen years ago at the age of 16. He is a global citizen renouncing on his U.S: citizenship with a tax plan in mind. Does exist as a matter of principle any rationale in imposing different conditions on natural persons compared to legal persons in a similar factual situation, having in mind the idea that these persons are interchangeable for the scope of the economic freedoms?

3. Cross-Border Movement of Companies

3.1. The devil is in the “formalities”

Within the EU there are as known two theories being used to determine the nationality of a legal person: the incorporation and the real seat theory. Member States enjoy the discretion to choose one or the other as a corporate nexus to a variety of laws applicable to a company. The central administration is the place where the main decisions are taken while the statutory seat is the official address of the company according to its statute. No matter which one is applicable, the companies wanting to transfer the corporate nexus, i.e. either their real or statutory seat, might be compelled to go into liquidation. Another denomination for corporate nexus is “*social seat*”.

The transformation of a company governed by the law of a Member State into a company governed by the law of another Member State presupposes two successive phases: administrative dissolution in the State of origin and incorporation in the State of destination. The first phase is governed by the law of the country where the dissolved company has its social seat and the second by the law of the country where the resulting company will be incorporated.

When a company is liquidated its assets and remaining liabilities will be distributed to the shareholders. On the contrary, when a company is dissolved without liquidation its assets and remaining liabilities will be directly transferred to the “*new-born*” creature of foreign law. The new company can be considered to constitute the legal successor of the dissolved one as in the case of a reincorporation since the assets are reintegrated under a new corporate shell.

A company dissolved without liquidation continues to own its assets and it continues to exist as a legal person though it has lost the status of corporation under the law of the Member State of origin; the dissolved company continues its legal existence though it cannot carry on any business within the Union until it achieves the status of corporation under the law of another Member State and whereby it regains the legal capacity to make binding amendments to its rights and obligations.

The Court has established in *Überseering* that denying the legal personality of a company having the registered office in another Member State amounted to an outright negation of the free establishment conferred under the Article 49 and 54 TFEU.³⁶

What about denying the legal personality of a company by the Member State of origin in relation to the intention of a domestic company to move the registered office to another Member State, acknowledging that the law of the latter allows the transfer? Would it also amount to an outright negation of the freedom of establishment? Is the right to universal transfer of assets at the time of the cross-border movement conferred by Union law?

3.2. Genuine exercise of the right of free movement of companies

The right of free establishment under Article 49 TFEU is guaranteed for companies that fulfil three cumulative conditions as laid down in Article 54 TFEU:

- a) Profit-making must be the pursuit of the activity without consideration of whether they actually succeed in making one or not;³⁷
- b) Formed under the civil or commercial laws of a Member State;
- c) A corporate nexus under the form of “*registered office, central administration or principal place of business*” within the Union.

The definition of the corporate nexus and the conditions under which a company is allowed firstly to obtain and secondly to retain the status of being incorporated under the law of a Member State is determined by the national company law of that Member State.³⁸

³⁶ Case C-208/00 *Überseering* para 93

³⁷ See *Cassa di Risparmio* Case C-222/04 para 123 where the Court found that being in competition with profit-making companies was enough in order to fulfil the conditions of “economic activity” i.e. any activity consisting in offering goods or services on a given market.

³⁸ Case C-371/10 *National Grid Indus*, paras 26-27

"*We are free because we live under civil laws*" in the words of Montesquieu. Are the companies free because they exist in a community based on rule of law as a constitutional guarantee stemming from the Treaties? Freedom of establishment is an integral part of the European legal order and the Member State of origin must in principle allow the emigration of companies incorporated under its laws, though the State of origin does not have to allow the emigrant to retain its legal status under its laws.³⁹

3.3. Identity of location for Registered and Central administration

Articles 49 and 54 TFEU secure the right of individuals and companies to move to another Member State to take up and pursue activities as self-employed persons and/or to set-up and manage undertakings in accordance with the conditions laid down in the law of that Member State for its own companies as well as to set up agencies, branches or subsidiaries in another Member State.

Does the cross-border transfer of registered office constitute a particular method of exercise of free movement of companies in the aftermath of *Sevic Systems*? Does this particular method constitute a genuine exercise of the right conferred even if the company continues to maintain the central administration and main economic activities in the Member State of origin?

According to *Cartesio* decision the transfer of central administration could be possible when it is followed by a change of applicable law.⁴⁰ This assertion can be interpreted in two ways: It could be either concluded that the location of central administration and registered office must be identical or that the power of the Member State to determine the corporation status is lost where the central administration and registered office are concurrently transferred to another Member State.

³⁹ Opinion of AG Kokott in C-371/10 National Grid Indus, point 35

⁴⁰ See also Article 8 of the SE Regulation

The European Parliament has recently noted that in the absence of provisions of Union law that prescribe which companies hold the right of establishment on the basis of a common corporate nexus determining the national law applicable to a company within the EU, the question whether Article 49 TFEU applies is a preliminary matter which, as Union law stands now, can only be decided by the applicable national law.⁴¹

It is still unclear whether or not the location of central administration and registered office must coincide in any situation. After *Cartesio* and *Grid Indus*, it has been established that as long as the company law of the State of origin allows the transfer of central administration to another Member State the situation falls within the scope of Article 49 TFEU and any conditions imposed, no matter their nature, will constitute restrictions that must be justified.

There are two types of preliminary matters that must be assessed in connection with cross-border movement of companies. The first is the status of legal person under the national law of the State of origin and the second relates to the legal provisions of the State of destination that stipulate requirements to be fulfilled with a view to formation or transformation of companies under its national law. Once the company is legally established under the law of the State of origin and the requirements for the company formation or transformation are in principle achievable according to the laws of the State of destination, all the additional conditions imposed on the transfer amount to restrictions of the economic freedoms, which might or not be justified and proportional.

⁴¹ European Parliament resolution of 23 November 2010 on civil law, commercial law, family law and private international law aspects of the Action Plan Implementing the Stockholm Programme (2010/2080(INI))

3.4. Legal and natural persons on an equal footing?

Kelsen argues that what is equal cannot be decided by the principle of equality.⁴² The principle seen alone is empty because it does not give any indications on what is similar situation and what is not. On the other hand the principle of equality before the law is addressed to the authorities applying the law in concrete situations. The legal personality i.e. the capacity to possess legal rights and duties is the foundation of the principle of equality before the law. Persons, legal and natural, are interchangeable for the scope of the freedom of establishment and therefore they are equal, not in character or abilities, but in all kind of activities related to establishment in another Member State.⁴³

De Lasteyrie and *N* are cases on taxation of natural persons applied on unrealized capital gains at the time of their emigration. The Court viewed the restrictions being precluded by Union law. In *De Lasteyrie* the restriction consisted in the provision of a guarantee and submission of the annual tax return. In *N* the tax deferral was granted only if collateral had been provided upon emigration.⁴⁴

Daily Mail stated that the transfer of central administration from UK to another Member State while maintaining the register office in the UK was not guaranteed by the Article 49(2) TFEU read in conjunction with 54 TFEU.⁴⁵ AG Kokott in *Grid Indus* brings a very helpful explanation of the famous paragraph in *Daily Mail*. The Member States have exclusive competence to determine the coming into existence of a legal person and the conditions to fulfil in order to retain legal status under national law.

⁴² Kelsen, H "What is justice?" Collected essays 1957 p 14

⁴³ Gribnau, H: Equality, Consistency and Impartiality in The Struggle for Equality in European Tax Law 2003 Kluwer Law International

⁴⁴ Case C-9/02 Hughes de Lasteyrie du Saillant v Ministère de l'Économie, des Finances et de l'Industrie and Case C-470/04 N. v Inspecteur van de Belastingdienst Oost/kantoor Almelo.

⁴⁵ Case 81/87 Daily Mail paras 24-25

A correct interpretation of *Daily Mail* leads to the conclusion that Member States have the power to deny a company to maintain the status of legal person under the national law in connection with a cross-border movement. Conversely, the Member States have no power to deny the transfer of companies that do not wish to retain the legal status.⁴⁶ In *Grid Indus* the immediate recovery of tax on unrealised capital gains relating to assets of a company transferring its place of central administration to another Member State at the very time of that transfer was disproportionate.⁴⁷

I underline already at this point that an outright denial and imposition of specific requirements, either ex-post or ex-ante, are two different things. Outright denial means that the transfer per se is not allowed by the national company law, while imposition of conditions would mean that the freedom is safeguarded but there are some conditions to be fulfilled either in advance or within a certain period of time.

Concerning natural persons there is no right to renounce citizenship according to ECHR and its protocols;⁴⁸ European Convention on Nationality⁴⁹ in Article 8 states that a Member State may refuse the renunciation if the applicant became stateless as a result of the loss of nationality. Conversely if the national has habitual residence abroad, the state of origin cannot refuse the renunciation.

However if we compare legal with natural persons and their renunciation rights under ECN, it's easy to draw a parallel: the State of origin can not oppose the renunciation, if the national has the habitual residence abroad and there is no risk for statelessness. Reconsidering *Daily Mail* and *Cartesio* in this context, it can be affirmed that the movement of companies can be opposed by the State of origin in cases where the company would become “*stateless*” as a result of the transfer. This would be the case if the State of destination did not allow the immigration.

⁴⁶ Opinion of AG Kokott in Case C-371/10 National Grid Indus point 23

⁴⁷ Case C-371/10 National Grid Indus, para 85

⁴⁸ ECtHR *Riener v Bulgaria* para 153

⁴⁹ Council of Europe Strasbourg, 6.XI.1997, paras 78-81

4. Secondary law in the field of free movement of companies

4.1. Regulation on Statute for a European Company

Neither the transfer of registered office to another Member State nor the conversion of an existing public limited-liability company into an SE as well as the conversion of an existing SE into a public limited-liability company shall result in the winding up of the company or in the creation of a new legal person.⁵⁰ According to the Opinion of AG Jääskinen in VALE, there are reasons to use by analogy the provisions of the existent secondary legislation as an advisory framework for other forms of cross-border transfer.⁵¹

Referring to taxation provisions applicable to a transfer of registered office or conversion the preamble stipulates that the SE-Regulation does not cover this area of law.⁵² Another important clause of the preamble prescribes that the transfer shall be neutral in relation to rights originating before the transfer.⁵³ The location of the central administration and registered office must nevertheless be identical.⁵⁴

If a company merely intends to move its registered office to another Member State can achieve this aim by first converting itself into a SE, then transfer its registered office to the target Member State and finally by reconverting the SE into a company governed by the law of the target. This series of company transformations would be disproportionately burdensome and time consuming. Just to give an example, the reconversion is allowed only after two years have elapsed from the first registration.⁵⁵

⁵⁰ Article 8(1) Article 37(2) and Article 66(2) of the SE Regulation

⁵¹ C-378/10 VALE Opinion of AG Jääskinen points 55-56

⁵² Preamble (20) of the SE Regulation

⁵³ Preamble (24) of the SE Regulation

⁵⁴ Article 7 and 64 of the SE Regulation

⁵⁵ Article 66(1) of the SE Regulation

4.2. Regulation on Statute for a European Cooperative Society

Exactly as in the case of a SE, cross-border transformations of a cooperative society shall not result in the winding-up or in the creation of a new legal person.⁵⁶ The registered office of a SCE shall be located within the Union, in the same Member State as its central administration.⁵⁷

The violation of the identity of location clause can result in a winding-up order issued by the court or other competent authority of the Member State where the SCE has its registered office.⁵⁸ In principle the SCE Regulation follows the same logic as the SE Regulation and the conclusion reached above concerning the unreasonable financial burden and time inefficiency is valid even in the case of cooperatives.

4.3. Regulation on Statute for a European Private Company

Companies with less than 250 employees and with a turnover of less than 50 million Euros or less than 43 million Euros in annual balance sheet have been defined as SMEs within the EU.⁵⁹ In 2008 the European Commission has proposed a new regulation meant to create a new European legal form, the European Private Company, in order to facilitate the cross-border establishment of SMEs.⁶⁰

The proposal does not regulate matters related to taxation. The choice of SPE as a legal form to conduct business activities in the EU should nonetheless be neutral from a tax perspective. It is hence imperative to ensure that the SPE enjoys the same tax treatment as similar national legal forms.⁶¹

⁵⁶ Article 7(1), Article 35(1), Article 76(2)

⁵⁷ Article 6 of the SCE Regulation

⁵⁸ Article 73 of the SCE Regulation (Concerning the SE positioning of seats, see Article 64 of the SE Regulation)

⁵⁹ Commission Recommendation 2003/361/EC concerning the definition of micro, small and medium-sized enterprises

⁶⁰ Proposal for a Council Regulation on the statute for a European private company, COM/2008/0396 final

⁶¹ Objectives of the SPE proposal, point 2

The transfer of the registered office of a SPE shall not result in the winding-up of the SPE or in any discontinuity of the SPE's legal personality or affect any right or obligation under any contract entered into by the SPE existing before the transfer.⁶² The SPE may be set up with its registered office and central administration or principal place of business in different Member States and consequently the shareholders would be allowed to transfer the registered office to another Member State while maintaining the central administration in the same location as before the transfer.⁶³

According to Article 4, the applicable law to a SPE is the SPE-Regulation itself and for matters falling outside the scope of the SPE-Regulation, the national law which applies to private limited-liability companies in the Member State in which the SPE has its registered office. The Article 5 prescribes that the law applicable to the transformation of a private limited-liability company into a SPE is the national law applicable to the transforming company. On the other hand, the formation of a SPE by transformation shall not give rise to the winding up of the company or any loss or interruption of its legal personality.⁶⁴

The formation of a SPE must be free of any restrictions. It may be set up by one or more founders, natural persons and/or companies or firms under Article 54 TFEU. Moreover, a European Company, a European Co-operative Society, a European Economic Interest Grouping or another SPE may also take part in the formation of an SPE. As already stated, the national law will merely govern those matters which are not covered by the SPE Regulation or by the articles of association of the SPE or fall outside the scope of company law as such.⁶⁵

⁶² Article 35(1) of the SPE Proposal

⁶³ Case C-212/97 Centros and Commission SPE- Proposal

⁶⁴ Article 5(2) of the SPE Proposal

⁶⁵ Chapter I: General provisions of the SPE Proposal

4.4. Cross-border mergers of limited liability companies

With respect to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, it is necessary to provide for tax rules which are neutral from the point of view of competition, in order to allow enterprises to adjust to the conditions of the internal market, to increase their efficiency and to improve their competitive power at the international level.⁶⁶

Merger is a transaction whereby on being dissolved without going into liquidation:

- a. At least one company transfers all assets and liabilities to another existing company, the acquiring company, in exchange for the issue to their members of securities or shares representing the capital of that other company and, if applicable, a cash payment not exceeding 10 % of the nominal value, or, in the absence of a nominal value, of the accounting par value of those securities or shares; or
- b. At least two companies transfer all their assets and liabilities to a company that they form, the new company, in exchange for the issue to their members of securities or shares representing the capital of that new company and, if applicable, a cash payment not exceeding 10 % of the nominal value, or in the absence of a nominal value, of the accounting par value of those securities or shares; or
- c. No more than one company transfers all its assets and liabilities to the company holding all the securities or shares representing its capital.⁶⁷

Only a common tax system, which would avoid the imposition of tax in connection with mergers, divisions, transfers of assets or exchanges of shares and concurrently safeguards the financial interests of the Member State of the transferring or acquired company, will provide an adequate solution in this respect.

⁶⁶ Preamble (2) Council Directive 2009/133/EC

⁶⁷ Article 2(2) of Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies

Member States are nevertheless allowed the possibility of refusing to apply the Directive⁶⁸ where the merger, division, transfer of assets, exchange of shares or transfer of the registered office of an SE or SCE has as its aim tax evasion or avoidance or results in a company, whether or not it takes part in the operation, no longer satisfying the conditions necessary for the participation of employees in company organs. A merger or division shall not give rise to any taxation of capital gains calculated by reference to the difference between the real values of the assets and liabilities transferred and their values for tax purposes.⁶⁹

4.5. Initiative 14th Directive on cross-border transfer of company seats

Articles 49 and 54 of the TFEU prescribe freedom of establishment for all companies. Cross-border company migration is one of the vital elements in the completion of the internal market and it should be tax-neutral. The lack of consistency in legislation on transfers and on procedures for transferring the registered office or central administration of an existing company incorporated under national law from one Member State to another, within the internal market, and the related risks in terms of employment, as well as the administrative difficulties, the costs generated, the social implications and the lack of legal certainty must be considered and dealt with by secondary legislation.

Exactly as the other acts of secondary legislation presented above, the initiative on the 14th Directive takes the view that the transfer must be allowed by dissolution without going into liquidation and the rights of the stakeholders originating before the transfer should be preserved. The transfer should not circumvent legal, social and fiscal conditions. The legislative provisions on employees' rights should be in line with the *acquis*. For the purposes of ongoing judicial or administrative proceedings which began before the transfer of seat, the company should be deemed as having its registered office in the State of Origin. Existing creditors should have the right to a security deposit.⁷⁰

⁶⁸ Article 15 of Council Directive 2009/133/EC

⁶⁹ Article 04 of Council Directive 2009/133/EC

⁷⁰ European Parliament resolution of 2 February 2012 with recommendations to the Commission on a 14th company law directive on the cross-border transfer of company seats

Conditions on transfer and conversion without liquidation are prescribed by secondary law provisions as previously enounced in this paper.⁷¹ In *VALE*, AG Jääskinen advocated that the removal from the Register in the State of origin shouldn't be effectuated before the company has been registered in the State of destination and the existent secondary law provisions could apply mutatis mutandis on the facts of the case in question; he emphasized nevertheless that in the absence of a specific provision it is the Court's mission to pave the way for the cross-border movement of companies.⁷²

⁷¹ SE Regulation and CBM Directive

⁷² Avocat général: Jääskinen Affaire C-378/10 points 40-42, 58, 79.

5. Abuse of economic freedoms- Substance over Form

5.1. Freedom of Establishment and Abuse of Law

A taxpayer enjoys the right to reduce the amount of what otherwise would be his taxes, or basically circumvent them by means allowed by law. However the law does not permit setting up artificial arrangements and devices of form meant to cover their real character as part of a preconceived plan to just obtain tax benefits. The pursuit of the principle of substance over form is to prohibit wholly artificial arrangements, which do not reflect economic reality and are set up with the sole aim of obtaining a tax advantage.⁷³

In *Marks & Spencer* the Court found that a national rule restricting deduction of cross-border losses could be theoretically justified by the risk of tax avoidance.⁷⁴ Conversely, the mere fact that a company transfers its place of management to another Member State could not set up a general presumption of tax evasion and justify a measure which compromised the exercise of the freedom of establishment.⁷⁵

5.2. Free Movement of Capital and Abuse of Law

It is true that nationals of a Member State cannot attempt, under cover of the rights created by the Treaties, to improperly circumvent their national legislation. A loss of fiscal revenues suffered by a Member State merely because a taxpayer has transferred its tax residence to another Member State, where the tax system is different and may be more favourable, cannot in itself justify a restriction of its fundamental freedoms.⁷⁶

⁷³ See, to that effect, Case C-162/07 *Ampliscientifica and Amplifin*, para 28

⁷⁴ Case C-446/03 *Marks & Spencer* para 51

⁷⁵ Case C-371/10 *National Grid Indus* para 84

⁷⁶ Case C-9/02 *De Lasteyrie de Saillant* para 60

They must not inappropriately or fraudulently take advantage of provisions of Union law.⁷⁷ Tax avoidance or evasion cannot be inferred generally from the fact that the tax residence of a natural person has been transferred to another Member State and cannot validate a fiscal measure which compromises the exercise of a fundamental freedom guaranteed by Union law.⁷⁸

In *Elisa* the Court observed nevertheless that two elements are necessary for a finding that a national measure governing the movement of capital between Member States is not caught by the justification of preventing tax avoidance. Firstly the Court underlined that Directive 77/799/EEC concerning mutual assistance by the competent authorities of the Member States in the field of direct and indirect taxation settled a general framework for cooperation and the exchange of information which supports each tax authority to combat fraud in cross-border situations.⁷⁹

Secondly, there is no reason why the tax authorities concerned should not request from the taxpayer the substantiation being required in order to accomplish an accurate evaluation of the taxes and duties in question and, where appropriate, decline the fiscal benefit if that evidence is not provided.⁸⁰

The case of transfer of tax residence is nevertheless a special situation; exit taxation in connection with this transfer is, as the law stands now, not precluded by Union law and furthermore it constitutes general practice even in jurisdictions outside the EU. This practice is in line with AG Darmon conclusion in *Daily Mail* that Member States should be allowed to impose exit taxation at the time of the transfer. Imposing a fiscal burden on the unrealized capital gains is a solution being compatible with the Union law as long as it does not render the transfer impossible or extremely difficult.

⁷⁷ Case C-196/04 Cadbury para 35

⁷⁸ Case C-9/02 Lasteyrie du Saillant para 51

⁷⁹ Case C-451/05 Elisa, paras 92-94

⁸⁰ Case C-451/05 Elisa, paras 95-96

In this context providing for a fiscal arrangement that confers an alternative to direct payment must be taken into consideration. A tax deferral granted at a reasonable rate of interest can constitute a sensible and accurate method to deal with the situation of change of tax residence and ensure protection for the economic freedoms of the taxpayers. The mutual assistance between the tax authorities within the framework for cooperation and the exchange of information shall facilitate the enforcement of this type of fiscal arrangement.

5.3. Transfer of Registered Office and Abuse of Law

In cases where the location of the central administration and the registered office coincide, the tax residence will also be situated in the same Member State and the question of tax avoidance will not arise. Conversely, in cases where a change of the registered office results in a change of the tax residence and the tax regime of the new residence is more favourable, the question of tax avoidance must be discussed. As shown above, whenever the change of tax regime is not the only purpose of the transfer of registered office, the circumvention is lawful.

In principle, a potential abuse of law by the controlling shareholders or their representatives shall be prevented, though a state measure that relies on a general presumption of abuse is clearly precluded by the Union law.⁸¹

From the economic point of view it is very easy to determine whether a change of location is no more than a formal change; any economic decision is an act of balancing potential earnings on one side against risks and costs on the other side. An illegal abuse occurs, where no economic risk is taken and no other future earnings are envisioned, except the avoidance of otherwise due taxes.

⁸¹ C-436/00 X and Y v Riksskatteverket, para 62

A transfer of assets, no matter their nature, tangible, intangible or financial, from one person to another involves an economic risk that must be counterbalanced by the expected return. The absence of risk or expected return gives a strong indication of the fact that the transaction lacks economic substance.

The transfer of registered office does not involve in itself a transfer of assets, but only a change of the applicable law similar with a change of nationality in the case of natural persons. Factually, it consists of changing the seat in the articles of association if the registered office is to be transferred, and of moving the headquarters if the central administration is to be transferred.

While obtaining a different nationality is a matter governed exclusively by the national law of the concerned State, renunciation of an already obtained nationality is a more complicated matter where companies are concerned; a company cannot hold double nationality as natural persons can. Does this renunciation imply an abuse of law?

6. Moving beyond Forms

6.1. Typology of Restrictions

6.1.1. Company law- Refusal to register the Transfer

The Court has upheld the diversity of national company laws already in *Daily Mail*.⁸² The restrictions originating in company law provisions relate to the loss of legal personality or ceasing to be incorporated under the law of the State of origin. In this context, two types of absolute restrictions can be envisaged: rules that invalidate the resolution approving the transfer adopted by the General Meeting of the Shareholders and rules that impose liquidation as a preliminary condition.

Certain Member States impose the condition of liquidation on companies that don't maintain an identical location for their central administration and registered office. This specific version embodies a prerequisite expressly requiring the company to transfer its central administration together with the registered office. If this type of preliminary condition imposed by a country applying the real seat theory appears to be legitimate, the situation is different concerning the countries applying the incorporation theory, which entails that the location of the central administration and registered office do not necessarily have to be identical.

I have to underline that the two doctrines invoked above aim to determine within the scope of national company law the location of the social seat of a domestic company. This doctrine is applied in order to ascertain whether or not a company is formally established under the relevant company law. Conversely, the connecting factors stipulated by the Brussels I Regulation decide the residence of a company for the purpose of determining the competent jurisdiction of courts. Even if these two sets of rules refer to exactly the same connecting factors, central administration, registered office/statutory seat and principal place of business, their function is obviously different.

⁸² Case 81/87 *Daily Mail* para 21

The idea to preserve the co-existence of the two differing theories has its own price; a non-transparent legal framework that contains a mixture of preliminary conditions must be penetrated before the cross-border operation can be commenced. The Union legislator concedes that there is a lack of consistency in the legislation on transfers and on procedures for transferring the registered office or central administration of an existing company incorporated under national law from one Member State to another. Therefore the range of restrictions that might be imposed lawfully is reduced considerably within the framework of the proposal for a SPE-Regulation.⁸³

6.1.2. Fiscal type of restrictions- Exit Taxation

For the transfer of central administration consent from the tax authorities is customarily required. In *Daily Mail*, an investment bank incorporated under the UK law sought to transfer its central administration to Netherlands. This was the first important case in relation to exit taxation and free movement of companies. In theory there are two restrictions that might be relevant, the double taxation of the property appreciation and the liquidity constraints related to taxes paid on unrealized capital gains. This paper is mainly concerned with the latter named type of restriction.

An illustrious example of exit taxation outside the Union jurisdiction is the one of the Facebook founder, Eduardo Saverin. Even if Mr Saverin is not European citizen, his fiscal situation provides a good example for the complexity of a decision concerned with the change of tax residence. Except the obvious fact that the State of destination provides for more favourable tax conditions, there is also an element of speculation and risk assessment referring to the difference between the future market price of the shares and their tax value at the time of the transfer. The decision to renounce the citizenship is not a merely formal one, but it has at least in this case an economic substance.

⁸³ Article 5.1 of the Proposal COM(2008) 396 final} {SEC(2008) 2098

In *National Grid Indus*, the Court emphasized that the national legislation at issue confined itself to attaching tax consequences, for companies incorporated under national law, for a transfer of the central administration between Member States, without the transfer affecting their status of companies under that law. It is necessary to provide for tax rules which are neutral from the point of view of competition, in order to allow enterprises to adjust to the conditions of the internal market, to increase their efficiency and to improve their competitive power on an international level.

Having in mind the idea of diversity in the context of fiscal environment, it is obvious that it's very difficult to achieve neutrality as long as the Member States retain a broad margin of discretion. A cross-border transfer of register office is not tax neutral, because the State of origin has the discretion to impose an exit tax on the company movement. This fiscal burden must be taken into consideration by the migrating company and be included in the costs of the transfer.

A company that ceases to retain the status of tax resident in a Member State is generally treated as having disposed of all of its assets at their market value at the time when this change occurs. Any capital gains arising as a result of this disposal are subject to tax.

Assets which continue to be used in the Member State of origin via a branch or agency of the company or where the company is ultimately controlled by residents of a tax treaty partner country are not subject to exit taxation. As it has been illustrated above, a change of the primary establishment of a domestic company results in a fiscal burden imposed on any capital gains registered at the time of the transfer. It is obvious that exit taxation decreases the wealth of a migrant company and indirectly the wealth of its shareholders, since there is no obligation on the Member States to ensure the fiscal neutrality of a cross-border transfer of registered office.

6.2. Is there a pearl inside this shell?

6.2.1. Transfer of registered office, a genuine economic activity?

Taxation and company incorporation rules fall within the competence of the Member States, though this competence must be exercised consistently with the Union Law.⁸⁴ Companies are accorded the freedom of establishment by Articles 49 and 54 TFEU. As the Union law currently stands, the State of origin has the discretion to determine the conditions and the level of taxation for different types of establishments chosen by national companies or partnerships operating abroad, on condition that foreign establishments of the national companies are not treated in a discriminatory manner in comparison with similar national establishments.⁸⁵

It is reasonable to assert that once the companies operating abroad cease to be established under the national law of the State of origin, the fiscal power enounced above does no longer exist. Having the formal seat and the real seat abroad, a company has no longer a connecting factor on the territory of the State of origin. In this specific situation the Member States impose an exit tax on the cross-border transfer as a usual fiscal measure. However in some cases the State opposes the transfer per se by invoking the principle of abuse of law.

Following the judgment of the Court in *Halifax*, it is unmistakable that the abuse of law principle, as established by the case-law of the Court prevents companies to rely on Union law for abusive or fraudulent purposes.⁸⁶ However the issue of abuse of law arises merely in cases where the concerned company has formally complied with the letter of law and therefore the interpretation of this principle cannot be extensive.⁸⁷

⁸⁴ Case C-157/10 Banco Bilbao Vizcaya Argentaria ECR 2011 I-0000, para 28

⁸⁵ Joined cases C-439/07 and C-499/07, *Belgische Staat v KBC Bank*, ECR 2009 I-04409 para 80

⁸⁶ Case C-255/02 *Halifax*, paras 69-73

⁸⁷ Case C-103/09, *Weald Leasing Ltd, AG Mazák* point 11

The test laid down by the Court in *Halifax* consists of two steps. Firstly, it must be established that the economic freedom is exercised in a way which would be contrary to the purpose of the relevant provisions and secondly that the essential aim of the transfer is to obtain a fraudulent benefit. If the company does not yet carry any operations abroad and still aims to transfer its register office towards another Member State, can this situation be qualified as an abusive attempt to avoid certain obligations imposed by the State of origin?

Articles 49 and 54 TFEU must be interpreted as precluding in principle a restrictive tax measure applied on the profits of a foreign establishment, which carries on genuine economic activities abroad.⁸⁸ This means that tax measures meant to nullify a tax advantage obtained by a resident company through its foreign establishments are generally precluded by Union law.

The respect for national diversity implies also that Member States shall recognize each other's corporate models. Acknowledging that the incorporation theory allows a company to have its real seat in a different Member State than the one of origin, the other Member States must allow the companies established in a Member State that applies this theory to set up their central administration within the Union in another Member State.

No matter if the transfer of registered office is considered to be an actual establishment from the perspective of the State of origin, as long as the State of destination defines the establishment as being genuine and lawful, the transfer of registered office will fall within the scope of the Article 49 TFEU. From the perspective of a Member State applying the incorporation theory, a company having the registered office on its territory satisfies the three cumulative conditions stipulated in Article 54 TFEU despite the fact that the central administration is located abroad.

⁸⁸ Case C-196/04 *Cadbury Schweppes* para 75

6.2.2. If the exercise is genuine which economic freedom would apply?

The objective of establishing or maintaining lasting economic links presupposes that the shares held by a shareholder enable him, either pursuant to the provisions of the national laws relating to companies, or in some other way, to participate effectively in the management of that company or in its control.⁸⁹ The Article 63(1) TFEU protects two types of right holders: potential investor and shareholder. The protection granted by this article is broader than the one granted by Article 49(2) TFEU. The latter covers only formation of primary and secondary establishments in another Member State and entrepreneurial direct investments.

Ultimately, in the present setting the persons protected are the majority shareholders. They have decided to execute a cross-border transfer or a conversion and any financial burden imposed on the exit may constitute a restriction liable to prohibit, impede or render less attractive the exercise of this freedom, all depending on the circumstances. In *VALE*, the Italian company has ceased to exist under the national law of the State of origin and the representatives of the shareholders' interests have established a new company under the Hungarian law.

Generally, the freedom of establishment has priority, where direct investments are involved, even if the restriction on the free establishment comes often as a consequence of an unfavourable treatment suffered by the direct investor. Where the Court has already found a restriction on the freedom of establishment, it considered that it was superfluous to scrutinize whether a particular measure also ran counter to the Treaty provisions on the free movement of capital.⁹⁰

⁸⁹ Case C-112/05 *Commission v Germany* para 18; See Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty [article repealed by the Treaty of Amsterdam]

⁹⁰ See, for example, Case C-118/96 *Safir*, para 35; Case C-200/98 *X and Y*, para 30; Case C-251/98 *Baars*, para 42; Joined Cases C-397/98 and C-410/98 *Metallgesellschaft and Others*, para 75; and Case C-436/00 *X and Y*, para 66.

The Court has not yet issued a judgment in the *VALE* case. However pure reasoning leads to the conclusion that a universal transfer of rights and obligations from the liquidated company towards the newly established one is not possible, since the new formed company didn't exist before the liquidation of the former. Thus the right holders in this case are the shareholders of the former Italian company and the relevant freedom refers to the right to re-establishment in Hungary.

6.2.3. Equal treatment in Art 54 TFEU and its practical relevance

Within the scope of freedom of establishment, 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 Union shall be treated in the same way as natural persons who are nationals of Member States, as stipulated by Article 54 TFEU.

Persons, legal and natural, are interchangeable for the scope of the free movement and therefore they are equal, not in character or abilities, but in all kind of activities related to establishment in another Member State. A State of origin may validly require taxpayers seeking permanently to leave its jurisdiction to settle their tax position, exit taxation, levied for instance, on unrealised capital gains, provided that it does not impose such exit taxes in a manner that is disproportionate to the necessity of securing fiscal coherence or avoiding abuse.⁹¹

In matters where equality of competition within the internal market might be concerned the legal form is not considered being an adequate indicator for the similarity of factual situations.⁹² In my opinion, the matter of establishment is closely connected with the preservation of free competition within the internal market and as I stated above, legal and natural persons in the position of investors and entrepreneurs are interchangeable; thus the choice of form should be a matter of managerial decision in order to allow enterprises to adjust to the conditions of trade, to increase their efficiency and to improve their competitive power at the international level.

⁹¹ Case C-9/02 *De Lasteyrie de Saillant* paras 63-69

⁹² Case C-222/04 *Cassa di Risparmio*, paras 135-136, 138, 152

The principle of substance over form in taxation aims to disregard differences of form and pursue to analyse the nature of a taxable transaction. Conversely the corporate law is essentially concerned with formalities and very seldom with the economic substance of a specific transaction. These two conflicting paradigms constitute a source of uncertainty in matters concerning the free movement of legal persons.

Nevertheless, the provisions of national corporate law govern preliminary matters related to the recognition and continuance of the legal personality of a company under the law of the State of origin and not the actual conditions of the cross-border movement. Once these preliminary conditions are fulfilled a migrating company must be treated in the same way as natural persons who are nationals of Member States.

6.2.4. Dissolution with liquidation and free movement of companies

A series of questions have arisen throughout this paper. Acknowledging that the law of the State of destination allows the immigration would denial of the legal personality of a domestic company with a view to its intention to transfer the registered office be precluded by Union law? Is the right to universal transfer of assets at the time of the cross-border movement conferred by Union law? Neither the Union secondary nor primary legislation contains provisions governing cross-border transformation of a company of a Member State or the international transfer of registered office of such company.⁹³

Where the transfer is allowed under the law of the State of destination, the denial by the State of origin of the legal personality of the migrating company has the effect of an absolute prohibition. The company as right holder ceases to exist and the eventual re-establishment in the State of destination can only be accomplished by the representatives of the shareholders exactly as is the case in *VALE*.

⁹³ C-378/10 *VALE* Opinion of AG Jääskinen point 4 referring to the proposal for a Directive on cross-border transfer of company seats.

Liquidation leads to the disintegration of the company's assets and to the discontinuity of its legal personality. Various justifications can be relevant and legitimate: protection of creditors, of employees, minority shareholders or prevention of fiscal avoidance. On the other hand, in most of the conceivable scenarios, less restrictive means would be available. For the case of taxation, the alternative solution is to impose an exit tax. The case-law highlights nevertheless that even this type of less restrictive means must be proportionate as the Court decision in *National Grid Indus* confirms.

Considering the other possible justifications referring to different safeguards of legitimate interests, the solutions envisaged by the provisions of the secondary legislation can serve as guiding norms. The proposal for the 14th Company Law Directive seems to follow indeed the same logic by establishing rules for the protection of third parties' interests and in the same time allowing the transfer by dissolution without liquidation. Nevertheless, the transfer should not affect the rights originating before the company movement or transformation.⁹⁴

I conclude by highlighting that even if the liquidation as a preliminary restrictive measure is not generally excluded, the application of such restriction in a specific case would be rarely if ever found to be proportionate. Company movement with change of applicable law is as a general rule governed by the law of the State of destination; the State of origin can impose preliminary conditions meant to provide protection for the third parties as long as these measures respect the proportionality principle.

⁹⁴ See for instance the Preamble of SE Regulation point 24

6.3. Conclusion

Internal market can be depicted as a system of rules governing all the possible cross-border transactions and this system must be effective and coherent. The internal market comprises a number of subsystems containing rules applicable in a specific national jurisdiction, including the so-called “*interfaces*” or in less metaphoric terms, the provisions determining the condition for entry and exit of companies. In this study the focus has been placed on a specific type of movement, namely the transfer of social seats, as a vehicle for cross-border transformations.

A change of tax residence, ensued from the transfer of social seat, is a decision that always must consider a complex set of causes and expected consequences, whereas fiscal liability constitutes only one of the critical factors. The applicable regulatory framework comprising several legal areas will be changed together with the social seat.

My conclusion in relation to this question is that a change of the tax residence through a cross-border transfer of registered office will always imply some additional consequences of non-fiscal nature. The latter named consequences might be beneficial as well, making the claim of tax avoidance as the only reason for the transfer simply refutable in a situation like that.

Besides the regulatory changes, the non-fiscal consequences include also valuation changes as shown by the accounting of assets before and after the transfer. Such differences must be disclosed and analysed carefully. The exit tax is finally determined at the time of the transfer when the company ceases to obtain profits taxable in the State of origin and the assistance of the State of destination won't concern its correct ascertainment, but only its possible recovery.⁹⁵ The principle of fiscal territoriality is related temporally to the moment when the State of origin loses all fiscal connection with the company.

⁹⁵ Article 4(1) of Council Directive 2008/55/EC of 26 May 2008

A decrease in the value of the transferred assets that occurs after the moment, when the fiscal connection is lost, does not impose any obligation on the State of origin to revalue the tax debt of the company. The Article 54 TFEU does not eliminate the disparities arising from national tax rules and thus does not ensure the fiscal neutrality of the transfer.⁹⁶

In this sense, I fully agree with AG Léger about the fact that a change of tax residence does not have any influence on the composition of assets and location of accounts and does not imply a transfer of ownership title. The change of tax residence per se is merely concerned with the allocation of fiscal powers between the Member States. A subsequent decrease in the actual assets value would only constitute a matter of fiscal accountability and the competence to grant an afferent recovery will exclusively belong to the State of destination.

On the other hand, company transformations constitute particular methods of exercising the freedom of establishment. In *SEVIC Systems* AG Tizzano explained that the pre-transformation phase, when the merging companies had different legal personalities, must be distinguished from the post-transformation phase, when we deal with only one legal entity having the personality of the State of destination.

Preventing a company established under the national law to participate in cross-border transformations constitutes a serious impediment against both the free movement of capital⁹⁷ and the freedom of establishment⁹⁸. A general refusal to register embodies an absolute form of prohibition comprising all forms of cross-borders movement of companies and a categorical impediment of the economic freedoms guaranteed by Union law. The prevention of cross-border movement by requiring the winding-up or liquidation of the migrating company is precluded by Article 49 TFEU, acknowledging that the laws of the State of destination permit the conversion.

⁹⁶ Case C-371/10 *National Grid Indus* paras 61-62

⁹⁷ Case C-222/97 *Trummer and Mayer* para 24; See also AG Tizzano in C-411/03 *Sevic Systems* point 76

⁹⁸ Case C-411/03 *SEVIC Systems*, para 31

What about the condition imposed by certain Member States and the SE- and SCE-Regulations to maintain the registered office and real seat at the same location in the same Member State? The sanction for not satisfying the condition of identity of location is as known the liquidation of the company. The key question which arises here is which law sets up the preliminary conditions that must be fulfilled in order to initiate the transfer. Is it the law of the State of origin or the law of the State of destination?

A cross-border conversion presupposes a change of the applicable law and it is for the State of destination to establish the prerequisites for the company transformation. The State of origin is nevertheless entitled to ensure the protection of the rights originating before the transfer, including here, its own taxation rights. In this exercise of power, rights guaranteed by the Treaty and rights enshrined in the national laws shall be correlated in a proportionality equation.

The liquidation belongs to the type of conditions meant to ensure protection of rights originating before the cross-border movement and even if it is not generally precluded by Union law, the application of such restriction in a specific case would be rarely if ever found to be proportionate and its lack of proportionality will render it illegal.

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