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THE MYSTERIES OF FREEDOM OF ESTABLISHMENT AFTER CARTESIO

CARSTEN GERNER-BEULER* AND MICHAEL SCHILLIG**

Abstract The judgment of the European Court of Justice in *Cartesio* was eagerly awaited as a clarification of the questions concerning the scope of the right of establishment (articles 49, 54 Treaty on the Functioning of the European Union (TFEU), (ex-articles 43, 48 EC) that remained after previous landmark decisions such as *Centros*, *Überseering*, and *Inspire Art*. This article analyses the implications of *Cartesio* in light of different scenarios of transfer of the registered and the real seat within the European Union. It assesses the interrelations of right of establishment and private international law rules for the determination of the law applicable to companies and concludes that the case law of the European Court of Justice after *Cartesio*, rather than providing for a coherent system of European company law, leads to arbitrary distinctions and significantly impedes the free movement of companies.

I. INTRODUCTION

Over the last decade, no one single issue seems to have occupied the minds of European company lawyers more than the question as to what extent companies formed under the law of a Member State may be able to enjoy the right to freedom of establishment. Three judgments handed down by the European Court of Justice at the turn of the millennium—*Centros*,¹ *Überseering*² and *Inspire Art*³—triggered an unprecedented amount of scholarly attention across Europe.⁴ Despite this intensive academic debate and a number of follow-up

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¹ Case C-127/97 *Centros Ltd v Erhvervs-og Selskabsstyrelsen* [1999] ECR, I-1459.

² Case C-208/00 *Überseering BV v Nordic Construction Baumanagement GmbH* [NCC] [2002] ECR I-9919.

³ Case C-167/01 *Kamer van Koophandel en Fabriken voor Amsterdam v Inspire Art Ltd* [2003] ECR I-10155.

⁴ eg H Halbhuber, 'National Doctrinal Structures and European Company Law' (2001) 38 CML Rev 1385; J Bisacre, 'The Migration of Companies within the European Union and the Proposed Fourteenth Company Law Directive' (2001) 3 ICCLJ 251; M Andenas, 'Free Movement of Companies' (2003) 119 LQR 221; E Wymeersch, 'The Transfer of the Company's Seat in European Company Law' (2003) 40 CMLR 661; F Wooldridge, 'Überseering: Freedom of Establishment of Companies Affirmed' (2003) 14 EBLR 227; S Lombardo, 'Conflict of Law

judgments, the ambit of the right to freedom of establishment for companies remained fairly uncertain, not least because often in the Court's decisions sweeping general pronouncements were supplemented by subtle distinctions. It is therefore no wonder that the Court's judgment in *Cartesio*⁵ was eagerly awaited as the latest piece of the puzzle. However, those who expected clarification will be bitterly disappointed. Instead of consolidating the right to freedom of establishment, the Court, in a judgment that in its English version is at times barely comprehensible, introduces new subtleties and complexities which will render freedom of establishment for companies a rather ineffective tool for the establishment of the Internal Market.

This article analyses the implications of *Cartesio* in light of different scenarios of transfer of the registered and the real seat within the European Union. It assesses the interrelations of right of establishment and private international law rules for the determination of the law applicable to companies and concludes that the case law of the European Court of Justice after *Cartesio*, rather than providing for a coherent system of European company law, leads to arbitrary distinctions and significantly impedes the free movement of companies.

II. FROM DAILY MAIL TO SEVIC

Where a company⁶ that was validly formed in a Member State (A) where it has its registered office is, according to the law of a second Member State (B), treated as having transferred to Member State (B) its central administration or principal place of business, the rules that Member State (B) imposes on and applies to the company will be subject to the right to freedom of establishment.⁷ Freedom of establishment can also be invoked by 'a company that was formed in one Member State only for the purpose of establishing itself in a second Member State where its main or indeed entire business is to be conducted.'⁸ This is definitely the case where the company's business in the second Member State is conducted via a registered

Rules in Company Law after Überseering: An Economic and Comparative Analysis of the Allocation of Policy Competence in the European Union' (2003) 4 EBOR 301; P Oliver and W-H Roth, 'The Internal Market and the four Freedoms' (2004) 41 CMLR 407; A Looijestijn-Clearie, 'Have the Dikes Collapsed? Inspire Art a Further Break-through in the Freedom of Establishment of Companies?' (2004) 5 EBOR 389; F Jacobs, 'The Evolution of the European Legal Order' (2004) 41 CMLR 303; G-J Vossestein, 'Exit Restrictions on Freedom of Establishment after Marks & Spencer' (2006) 7 EBOR 863; F Mucciarelli, 'Company 'Emigration' and EC Freedom of Establishment: Daily Mail Revisited' (2008) 9 EBOR 267.

⁵ Case C-210/06 *Cartesio Oktató Szolgáltató* bt [2008] ECR I-9641.

⁶ cf art 54(2) TFEU (ex-art 48(2) EC): the wording of this provision is misleading ('and other legal persons'); it covers entities that enjoy separate legal personality as well as civil or commercial partnerships that under the applicable law are not afforded separate legal personality.

⁷ Überseering (n 2) para 52.

⁸ Inspire Art (n 3) para 95; referring to Centros (n 1) para 17, and Case 79/85 *Segers* [1986] ECR 2375 para 16.

branch⁹ (in a strictly formal sense).¹⁰ However, given the decision in *Überseering* and the inclusive language used in *Inspire Art*,¹¹ freedom of establishment also seems to apply where the company's establishment in the Member State of destination is the company's only establishment. Registration of a branch in the Member State of destination, therefore, does not seem to be a necessary prerequisite for enjoying the protection of freedom of establishment. Finally, cross-border merger operations have been held to 'constitute particular methods of exercise of the freedom of establishment, important for the proper functioning of the internal market'.¹² Thus, Member States are prevented from treating a merger between companies differently depending on the internal or cross-border nature of the merger.¹³

What remained unresolved until now was the question of whether provisions of the Member State of incorporation which rendered the departure of a company impossible or more burdensome were also subject to freedom of establishment scrutiny. In *Daily Mail*¹⁴ the Court held that 'in the present state of Community law', articles 49, 54 Treaty on the Functioning of the European Union (TFEU) (ex-articles 43, 48 EC) 'cannot be interpreted as conferring on companies incorporated under the law of a Member State a right to transfer their central management and control and their central administration to another Member State while retaining their status as companies incorporated under the legislation of the first Member State.' After *Überseering*¹⁵ and *Inspire Art*,¹⁶ this statement could claim validity only in respect of the 'relations between a company and the Member State under the laws of which it had been incorporated' and whose laws restricted the company's mobility. For this particular situation, neither in *Überseering* nor in *Inspire Art* did the Court in any way depart from *Daily Mail*. Rather, the Court seemed to differentiate between the question of applicability of freedom of establishment, on the one hand, and the preliminary question of whether the company was validly formed, and remained in existence, under the law of a Member State, on the other. This is because 'unlike natural persons, companies are creatures of the law and, in the present state of Community law, creatures of national law. They exist only by virtue of the varying national legislation which determines their incorporation and functioning.'¹⁷

⁹ Eleventh 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 [1989] OJ L 395/36.

¹⁰ *Centros* (n 1) para 17; *Inspire Art* (n 3) para 97.

¹¹ *Inspire Art* (n 3) para 95–96.

¹² Case C-411/03 *SEVIC Systems AG* [2005] ECR I-10805 para 19.

¹³ *SEVIC* (n 12) para 31.

¹⁴ Case 81/87 *The Queen v HM Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust plc* [1988] ECR 5483 para 24.

¹⁵ *Überseering* (n 2) para 61–73.

¹⁶ *Inspire Art* (n 3) 103.

¹⁷ *Daily Mail* (n 14) para 19.

Doubts were raised in *Lasteyrie du Sallant* where the ECJ held that article 49 TFEU (ex-article 43 EC) ‘also prohibits the Member State of origin from hindering the establishment in another Member State of one of its own nationals’ and consequently precludes a Member State from establishing, in order to prevent a risk of tax avoidance, a mechanism for taxing as yet unrealized increases in value, where a taxpayer transfers his tax residence outside that State.¹⁸ However, the case did not represent a clear departure from *Daily Mail* because it dealt with a natural person whose legal and natural existence clearly does not depend on the legal order of its home Member State.

In *Marks & Spencer* the Court went one step further and held that the provisions concerning freedom of establishment also ‘prohibit the Member State of origin from hindering the establishment in another Member State . . . of a company incorporated under its legislation.’¹⁹ A national rule which allows a parent company to set-off losses incurred by resident subsidiaries, but not the losses incurred by subsidiaries incorporated in another Member State, was found to constitute a restriction²⁰ to freedom of establishment by deterring the parent company ‘from setting up subsidiaries in other Member States’.²¹ Again, the *Daily Mail* reasoning remained unscathed because the setting up by a company incorporated in one Member State of a subsidiary in another Member State (secondary establishment) does not affect the parent company’s existence as a ‘creature of the law’ of the Member State of incorporation.

As for the cross border merger context, the Court’s decision in *SEVIC* seemed to suggest that the different treatment of a merger that involves a foreign company as compared to a purely domestic merger always amounts to a restriction of the right of establishment irrespective of whether the different treatment emanates from the Member State of the absorbing entity or the Member State of the absorbed entity.²² This appeared to signal a significant departure from *Daily Mail*, at least as far as discriminatory measures were concerned. However, the fact remains that in *SEVIC* registration was refused by the Member State of the absorbing entity and, therefore, arguably by the country of destination.

¹⁸ Case C-9/02 *Lasteyrie du Saillant* [2004] ECR I-2409 para 42.

¹⁹ Case C-446/03 *Marks & Spencer plc v HM's Inspector of Taxes* [2005] ECR I-10837 para 31.

²⁰ The Court held that the restriction was justified to the extent that the losses incurred by the non-resident subsidiary could be taken into account in the subsidiary’s State of residence.

²¹ *Marks & Spencer* (n 19) para 33.

²² *SEVIC* (n 12) para 31: ‘Articles 43 EC and 48 EC 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 registration is possible, . . . , where the two companies participating in the merger are both established in the territory of the first Member State.’

In light of these uncertainties and in order ‘to improve the efficiency and competitive position of European companies by providing them with the possibility of transferring their registered office more easily’ so that they can ‘choose a legal environment that best suits their business needs’ the Commission contemplated a directive on the cross border transfer of a company’s registered office.²³ However, following a consultation process, the Commission’s impact assessment concluded that it was not clear whether adopting a directive would represent the least onerous way of achieving the objectives pursued. The Commission argued that the practical impact of the existing legislation on cross-border mobility²⁴ was not yet known and the issue of the transfer of the ‘registered office’ might be clarified by the Court in *Cartesio*.²⁵ Following the impact assessment, Commissioner McCreevy decided there was no need for action at EU level. DG Internal Market and Services has therefore stopped work on legislation in this area.

III. CARTESIO

The *Cartesio* case was enveloped in the mist of confusion right from the start. According to the English translation of the reference for a preliminary ruling, the Hungarian court seemed to ask whether a company that wished to transfer its ‘registered office’ to another Member State could invoke the right to freedom of establishment. The German translation referred to the ‘*Sitz*’ of the company, the French translation to the ‘*siege social*’. Under the Companies Act 2006, the ‘registered office’ is relevant as the place where documents may be served²⁶ and where a company may keep registers and certain documents for inspection.²⁷ It does not have to be located where the company has its operational headquarters or principal place of business. Conversely, ‘*Sitz*’ in Germany²⁸

²³ The Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, Brussels, 2002, 20, urged the Commission to bring forward a revised proposal for a Fourteenth Directive on the Transfer of the Registered Office. In its Communication to the Council and the European Parliament on modernising company law and enhancing corporate governance in the European Union—A plan to move forward, COM(2003)284 final, 20, the Commission expressed its intention to present a new proposal for a Fourteenth Directive in the short term.

²⁴ Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies [2005] OJ L310/1.

²⁵ Commission Staff Working Document: Impact assessment on the Directive on the cross-border transfer of registered office, 12.12.2007, SEC(2007) 1707, 5–6.

²⁶ Companies Act 2006, s 1139(1).

²⁷ Companies Act 2006, s 1136. Alternatively, the records may be kept at some other place permitted by regulations to be made under Companies Act 2006, s 1136.

²⁸ GmbHG, § 4a(2); AktG, § 5(2), as in force until 30 October 2008. In light of the right to freedom of establishment and in order to create a level playing field for domestic companies, Germany has already changed its law in this respect. Since 1 November 2008, German private and public companies may choose their operational headquarters freely within the Community. Only the registered office as stipulated in the articles of association must be situated in Germany. cf Gesetzentwurf der Bundesregierung: Entwurf eines Gesetzes zur Modernisierung des

and ‘*siege social*’ in France²⁹ traditionally have to coincide with the place from where the company is actually being run. The English translation of the reference seems to have influenced the Commission’s impact assessment where it was assumed that *Cartesio* was about the transfer of the ‘registered office’.³⁰ It also prompted the Irish government to request the re-opening of the oral procedure³¹ after Advocate General Maduro had delivered his opinion based on a transfer of the real seat.³²

However, from the Advocate General’s opinion the facts seem to be reasonably clear: *Cartesio* was a limited partnership formed in accordance with Hungarian law and registered in Hungary. When it submitted an application to the commercial court to amend its registration in the local commercial register so as to register an address in Italy as its new operational headquarters, the court rejected the application on the ground that Hungarian law did not permit companies to transfer their operational headquarters to another Member State while retaining their legal status as a company governed by Hungarian law. In order to change its headquarters, *Cartesio* would have to dissolve in Hungary first and then re-incorporate under Italian law. When *Cartesio* appealed against the decision of the commercial court, the Court of Appeal referred a number of questions to the ECJ for a preliminary ruling. As far as the right to freedom of establishment is concerned, the Hungarian court essentially asked whether articles 49, 54 TFEU (ex-articles 43, 48 EC) are to be interpreted as precluding national legislation which prevents a company from transferring its operational headquarters to another Member State whilst retaining its status as a company governed by the law of the Member State of incorporation.³³

Based on the order for reference, the Advocate General assumes that Hungarian law is grounded in the ‘real seat’ theory.³⁴ Under Hungarian law, the place of a company’s operational headquarters is supposed to coincide with its place of incorporation. Thus, Hungarian company law prohibits the ‘export’ of a Hungarian legal person to the territory of another Member State. This, according to Advocate General Maduro, is within the scope of the right of establishment.³⁵ The Advocate General’s first argument is essentially

GmbH-Rechts und zur Bekämpfung von Missbräuchen (MoMiG), BR-Drucksache 354/07, 25 May 2007, 65, 65 and Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Mißbräuchen (MoMiG), 23.10.2008, BGBl. 2008, I Nr. 48, 2026. Current Hungarian law contains a similar rule in regard to movements within the European Union, art 7/B. of Law No V of 2006 on Public Company Information, Court Registration Proceedings and Voluntary Dissolution Proceedings (2006. évi V. törvény a cégnyilvánosságról, a bírósági cégeljárásról és a végelszámolásról).

²⁹ P Merle, *Droit commercial: Société commerciales* (11th edn, Paris, Dalloz, 2007) para 83.

³⁰ Commission Staff Working Document (n 25) 5.

³¹ *Cartesio* (n 5) para 41–53.

³² AG Maduro, opinion in Case C-210/06 *Cartesio Oktató Szolgáltató bt* [2008] ECR I-9641, para 2–4.

³³ *Cartesio* (n 5) para 99.

³⁴ On the correctness of this assumption under Hungarian law, see further discussion (n 97).

³⁵ AG Maduro (n 32) para 23.

derived from the Court's reasoning in *SEVIC*: 'National rules that allow a company to transfer its operational headquarters only within the national territory clearly treat cross-border situations less favourably than purely national situations. In effect, such rules amount to a discrimination against the exercise of freedom of movement.'³⁶ In a second step, the Advocate General rejects the *Daily Mail* reasoning³⁷ and refutes efforts which try to distinguish *Daily Mail* from *Centros*, *Überseering* and *Inspire Art* on the facts.³⁸ Given that the right to freedom of establishment 'also prohibits the Member State of origin from hindering the establishment in another Member State of one of its own nationals,'³⁹ distinctions based on aspects of primary as opposed to secondary establishment and inbound versus outbound establishment were, according to the Advocate General, never entirely persuasive.⁴⁰ Under the general analytical framework, the Court would not 'a priori' exclude particular areas of national law from the scope of the right of establishment.⁴¹ Although Member States were free to organize their national company laws along the lines of real seat theory or incorporation theory, freedom of establishment required a minimum degree of mutual recognition and coordination of these various systems of rules so that neither theory could be applied to its fullest extent.⁴² Consequently, it was

impossible, [...], to argue on the basis of the current state of Community law that Member States enjoy an absolute freedom to determine the 'life and death' of companies constituted under their domestic law, irrespective of the consequences for the freedom of establishment. Otherwise, Member States would have carte blanche to impose a 'death sentence' on a company constituted under its laws just because it had decided to exercise the freedom of establishment.⁴³

Because of the costs and administrative burdens inherent in first having to wind up the company in its country of origin and then to re-establish it completely in the country of destination, national rules that prevent an intra-EU transfer of the operational headquarters amounted to a restriction on freedom of establishment.⁴⁴ This restriction may be justified on grounds of general public interest. However, since the Hungarian rules 'completely deny' a Hungarian company to transfer its operational headquarters to another Member State it was, according to the Advocate General, 'difficult to see how such "an outright negation of the freedom of establishment" could be necessary for reasons of public interest.'⁴⁵

The Court did not follow the path recommended by Advocate General Maduro. In fact, it is not entirely clear whether the Court followed any path at all. The Court's starting point is its reasoning in *Daily Mail*: '[C]ompanies are

³⁶ *ibid* para 25.

³⁷ *ibid* para 26.

³⁸ *ibid* para 28.

³⁹ Case C-251/98 *Baars* [2000] ECR I-2787, para 28; Case C-9/02 *Lasteyrie du Saillant* [2004] ECR I-2409, para 42, to which AG Maduro (n 32) refers in note 48 of his opinion.

⁴⁰ AG Maduro (n 32) para 28.

⁴¹ *ibid* para 30.

⁴² *ibid* para 30.

⁴³ *ibid* para 31.

⁴⁴ *ibid* para 32.

⁴⁵ AG Maduro (n 32) para 34.

creatures of national law and exist only by virtue of the national legislation which determines [their] incorporation and functioning.⁴⁶ Article 54 TFEU (ex-article 48 EC) takes into account that national laws vary widely as to the connecting factor required for incorporation and the subsequent modification of that factor.⁴⁷ From this, the Court inferred in *Überseering* that a Member State could restrict a company's right to retain its legal personality under its law when its centre of administration was transferred to a foreign country.⁴⁸ Moreover, it considered article 54 TFEU (ex-article 48 EC) to leave the question of the connecting factor and its subsequent change as unresolved by the rules on freedom of establishment, and to reserve these issues for further legislation.⁴⁹ Consequently, 'in the absence of a uniform Community law definition of the companies which may enjoy the right of establishment on the basis of a single connecting factor determining the national law applicable to a company', the question whether a company actually has the right to freedom of establishment is 'a preliminary matter which, as Community law now stands, can only be resolved by the applicable national law.'⁵⁰

Thus, 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.⁵¹ This seems to follow logically from the Court's premise quoted above. Companies validly 'formed in accordance with the law of a Member State' are to be awarded equal status with natural persons and can rely on freedom of establishment. From the point of view of the company, the definition of the connecting factor (that determines the applicable law) is a matter for national law and immune from freedom of establishment interference in the same way as are domestic substantive and procedural rules on company formation. This conceptually clear picture becomes somewhat blurred, however, if one looks at it from the perspective of the company's founders. Their right to freedom of establishment includes the right 'to set up ... companies'.⁵² Article 49 TFEU (ex-article 43 EC) confers this right only under the conditions laid down by the host Member State for its own nationals. However, in line with the Court's case law on the market freedoms in general,⁵³ the ECJ has extended the scope of freedom of establishment so as to encompass national measures which are 'liable to hinder or make less attractive' the exercise of freedom of establishment.⁵⁴ If the founders could invoke this freedom in order to challenge

⁴⁶ *Cartesio* (n 5) para 104.

⁴⁹ ibid para 108.

⁵² cf art 49 TFEU (ex-art 43 EC); W Schön, 'Niederlassungsfreiheit als Grundungsfreiheit' in P Hommelhoff, P Rawert and K Schmidt (eds), *Festschrift für Hans-Joachim Priester zum 70. Geburtstag* (Dr Otto Schmidt, Köln, 2007) 737, 739–743.

⁵³ Case 8/74 *Dassonville* [1974] ECR 873 (free movement of goods); Case C-76/90 *Säger* [1991] ECR I-4221 (freedom to provide services); Case C-415/93 *Bosman* [1995] ECR I-4921 (free movement of workers); art 63 TFEU (ex-art 56 EC) explicitly refers to 'restrictions on the movement of capital between Member States and between Member States and third countries'.

⁵⁴ Case C-55/94 *Gebhard* [1995] ECR I-4165, para 37.

⁴⁷ ibid para 105–106.

⁵⁰ ibid para 109.

⁴⁸ ibid para 107.

⁵¹ ibid para 110.

the connecting factor for incorporation required by a Member State, they could equally challenge the substantive rules on company formation. Freedom of establishment does not differentiate between substantive law and conflict of laws rules. This would mean the end of national company law as we know it. The content of large areas of substantive company law would have to be deduced directly from freedom of establishment. Therefore, in accordance with the rationale in *Keck*,⁵⁵ conflict of laws and substantive company law rules that ‘apply to all relevant traders operating within the national territory’ and ‘affect in the same manner, in law and in fact’ domestic entrepreneurs and those from other Member States should be deemed to fall outside the scope of freedom of establishment. Such provisions do not specifically impede market access by foreign incorporators more than they impede company formation by domestic ones.⁵⁶ Thus, so long as applied in a non-discriminatory manner, substantive company law seems to be safe. As regards the requirement of having the operational head office in the Member State of incorporation, it could be argued that it will be more difficult for foreign founders to establish a physical presence in the Member State of incorporation, thus treating them differently at least in fact. Such a requirement may, therefore, only stand if justified by imperative requirements in the public interest.⁵⁷

Secondly, according to the Court, the Member State also has the power to prevent a company governed by its law from retaining that status if the company intends to move its seat to the territory of another Member State, ‘thereby breaking the connecting factor required under the law of incorporation’.⁵⁸ This result does not follow logically from the *Daily Mail* reasoning. With the company established as a legal person it is hard to see why freedom of establishment should not apply. The company was formed in accordance with the law of a Member State and would still have its registered office, central administration or principle place of business within the EU. As a result of the Court’s reasoning, Member States are unconstrained by the right to freedom of establishment, not just in respect of the connecting factor for incorporation and formation, but also in respect of decisions taken by lawfully established companies to the extent that the company intends to remain subject to the law of incorporation.

Now the Court distinguishes this situation (of a company moving its seat to another Member State whilst retaining its status as company under the law of the Member State of origin) 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.⁵⁹ In that case, the Member State’s power to

⁵⁵ Joined cases C-267 and 268/91 *Keck and Mithouard* [1993] ECR I-6097.

⁵⁶ cf Case C-384/93 *Alpine Investment BV v Minister van Financiën* [1995] ECR I-1141, para 37.

⁵⁸ *Cartesio* (n 5) para 110.

⁵⁷ *Gebhard* (n 54) para 37.

⁵⁹ *ibid* para 111.

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.’⁶⁰ 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 to freedom of establishment which, unless justified by overriding requirements in the public interest, will be prohibited under article 49 TFEU (ex-article 43 EC).⁶¹ This result seems to be in accordance with, and even to go beyond, the rules the Commission contemplated for a Fourteenth Company Law Directive on the cross-border transfer of a company’s registered office. In its online consultation, the Commission suggested that each Member State should recognize the right of a company governed by its national law to transfer its registered office to another Member State in order to acquire a new legal personality. The host Member State should not be allowed to refuse to register a company which satisfies the essential substantive and formal requirements for the registration of national companies. It may however provide as a substantive requirement that the company’s registered office and operational head office coincide.⁶² It is also in line with the rules governing the transfer of the entity seat to another Member State laid down by Regulation 2157/2001 on the European Company,⁶³ and Regulation 1435/2003 on the European Cooperative Society.⁶⁴ Under these rules an entity can transfer its registered office and its real seat—which both must be situated in the same country⁶⁵—to another Member State.⁶⁶ Such a transfer entails a change in the applicable law.⁶⁷ In fact, the Commission argued that the rules that govern the transfer of the seat of these supra-national entities could and should be applied ‘*mutatis mutandis*’ to the cross-border transfer of the real seat of companies created under domestic law. However, since *Cartesio* intended to remain a Hungarian company, these

⁶⁰ *ibid* para 112.

⁶¹ *ibid* para 113.

⁶² For this consultation process and the Commission’s suggestions cf http://ec.europa.eu/internal_market/company/seat-transfer/2004-consult_en.htm (last visited 6 April 2009).

⁶³ Regulation (EC) 2157/2001 of 10 August 2001 on the Statute for a European Company (SE) [2001] OJ L 294/1, supplemented by Directive 2001/86/EC of 10 August 2001 on employee participation [2001] OJ L 294/22.

⁶⁴ Regulation (EC) No 1435/2003 of 22 July 2003 on the statute for a European co-operative society (SCE) [2003] OJ L 207/1, supplemented by Directive 2003/72/EC of 22 July 2003 on employee participation [2003] OJ L 207/25.

⁶⁵ Regulation (EC) 2157/2001, art 7; Regulation (EC) No 1435/2003, art 6.

⁶⁶ Regulation (EC) 2157/2001, art 8; Regulation (EC) No 1435/2003, art 7.

⁶⁷ Regulation (EC) 2157/2001, art 9(1)(c)(ii)(iii); Regulation (EC) No 1435/2003, art 8(1)(c)(ii)(iii). Council Regulation (EEC) 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG) [1985] OJ L 199/1 follows somewhat different rules. Although the official address must be at the place where the grouping has its central administration or where one of the members has its central administration (art 12), the official address may be transferred within the Community with or without change in the applicable law (Art. 13, 14).

provisions—which result in a change in the applicable law—could not be applied *mutatis mutandis* in order to support the applicant's case.⁶⁸

Lastly, the Court clarified the ambit of *SEVIC*. The situation in *SEVIC*, according to the Court, 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*⁶⁹ and could not be of assistance in a case like *Cartesio*.

For these reasons, the Court held that articles 49, 54 TFEU (ex-articles 43, 48 EC) '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.'⁷⁰ This ruling considerably increases complexity of the right to freedom of establishment. Whether a company and its owners and management may rely on freedom of establishment appears to be intrinsically linked to, and dependent upon, the structure not just of the conflict of laws rules adopted by the affected Member States, but also their substantive company laws.

IV. APPLICABLE COMPANY LAW MOVES IN MYSTERIOUS WAYS

We will now analyse several cases in which a company seeks to transfer its real or registered seat from the Member State of incorporation (Member State A) to another Member State (Member State B). These cases, which will be based on different combinations of conflict of laws and substantive company law rules, will show that the criteria developed by the Court of Justice to delineate the scope of application of articles 49, 54 TFEU (ex-articles 43, 48 EC) lead to arbitrary results and lack an intrinsic justification.

Case 1: Assume first that Member State A follows the incorporation theory and that the company wishes to transfer its real seat to Member State B. This is the case that was decided in *Cartesio*.⁷¹ If the company law of Member State A stipulates that the centre of administration of the company must be located in A (again as in *Cartesio*), the real seat cannot be transferred to B without dissolution and liquidation of the company.⁷² If the company law of Member State A is more liberal, thus not requiring real seat and registered office to be situated within its territory,⁷³ A's law does not require dissolution and *Cartesio* does not have a bearing on the case. Now the conflict of laws rules of the receiving State are of relevance. Under the incorporation theory, the courts

⁶⁸ *Cartesio* (n 5) para 115–120.

⁶⁹ *ibid* 121–123.

⁷⁰ *ibid* para 124.

⁷¹ AG Maduro comes to the conclusion that Hungarian company law follows the real seat theory (n 32) para 23. However, this conclusion does not seem to be in accordance with the respective Hungarian provisions. See further (n 97).

⁷² cf the holding in *Cartesio* (n 5) para 110.

⁷³ cf (n 28).

in Member State B will apply A's law, consequently treating the company as a validly incorporated (foreign) legal entity. The real seat theory would lead to a different result. The courts in Member State B would apply their own (substantive) company law. Since the company was not formed under B's laws, it would need to dissolve and re-incorporate. However, this consequence has been enjoined in *Überseering*: A company that has been validly formed under the laws of one Member State and that transfers its real seat to another Member State has to be recognized by that second State. Again, the company is permitted to retain its character as a company under A's laws.

Case 2: The legal situation is different if the company seeks to transfer its registered seat from a Member State applying the incorporation theory (A) to another State (B). As discussed above, the Court of Justice is of the opinion that this case falls within the reach of articles 49, 54 TFEU (ex-articles 43, 48 EC). The Member State of incorporation may not require the winding-up or liquidation of the company. Instead, the company must be able to convert into a form of company governed by the law of the other State.⁷⁴ A receiving Member State that follows the incorporation theory will judge the case according to its own company law. It may require re-incorporation of the company before it can take up business as a valid legal entity in that State. Such prohibitive rules are not in contradiction to the right of establishment. First, *Cartesio* makes clear that the continued existence of the company is only guaranteed, ie articles 49, 54 TFEU (ex-articles 43, 48 EC) only safeguard the right of a company to convert itself into a company governed by another legal system, to the extent that the law of the receiving State allows the conversion.⁷⁵ Second, the dictum of *Überseering* is restricted to the case of a company 'which is validly incorporated in one Member State ('A') in which it has its registered office [and which] is deemed, under the law of a second Member State ('B'), to have moved its actual centre of administration to Member State B'.⁷⁶ In other words, the laws of Member State B are not reviewed in light of articles 49, 54 TFEU (ex-articles 43, 48 EC) unless the legal existence of the company in Member State A is established.⁷⁷

If B is a real seat State the analysis is as follows. We assume that the real seat of the company has remained in A and the company has applied for registration in B to take advantage of B's company law, which might be more liberal or more suitable for the particular purposes of the company.⁷⁸ Jurisdiction of the registration court or office is determined in accordance with

⁷⁴ *Cartesio* (n 5) para 112.

⁷⁶ *Überseering* (n 2) para 52.

⁷⁸ This assumption might not be of great practical relevance. Market actors that wish to take advantage of the regulatory regime in B will presumably incorporate in B in the first place and conduct all business operations in A, which is the *Centros* scenario (but cf Oberlandesgericht [Higher Regional Court] Zweibrücken, Wertpapiermitteilungen (WM) 2005, 2140: transfer of the registered seat of an association formed under French law from France to Germany). However, for expository purposes all alternatives of a transfer of seat shall be analysed in light of the case law of the ECJ.

⁷⁵ *ibid* para 112.

⁷⁷ *ibid* para 63.

the procedural law of the State where the court or office is located. Since procedural jurisdiction is a question of public law and, consequently, territoriality, the private international law rules of the Member State and the law applicable to the company are, at this point of the analysis, irrelevant.⁷⁹ Thus, the national law of the receiving Member State determines *where* registration after transfer and conversion into a type of company governed by that State's law is permitted. In general, the registration court or office in whose district the (new) registered seat of the company will be located has jurisdiction.⁸⁰ However, the question of *whether* transfer of seat and conversion without dissolution and re-incorporation is permissible is one of substantive law; accordingly, private international law rules determine the applicable law. The real seat State refers to the law of the incorporation State (A), which will accept the remission regarding the dissolution of the corporation and probably refer back to B for the question of re-incorporation.⁸¹

Now, *Cartesio* stipulates that A cannot restrict the movement of the company from A to B if the transfer entails a change in the applicable law (which is, in this example, the case). The company does not need to be wound up, and the company may (depending on B's company law concerning transfers of seat from abroad) be registered in B. Or so it would seem. Consider, as mentioned above, that according to *Cartesio* A is not allowed to require winding-up and liquidation if the company 'is permitted under [the] law'⁸² of B to convert. B's law, on the other hand, applies A's company law, which would require dissolution if that was not prohibited under *Cartesio*. As can be seen, the principles established by the ECJ lead to a circular argument. The conundrum may be solved by assuming that *Cartesio* refers only to the substantive law of the receiving State or that B's remission already implements the principles of *Cartesio*, ie does not apply A's law to the extent that it requires dissolution.

To summarise, in both cases (transfer of the registered seat from an incorporation theory country to another incorporation theory country or to a real seat country) Member State A is enjoined from requiring dissolution, but the company may need to re-incorporate under the substantive company law of Member State B.⁸³ In the second case (transfer into a real seat country) this

⁷⁹ cf P Mankowski and OL Knöfel, 'Registrierung' [Registration] in H Hirte and T Bücker (eds), *Grenzüberschreitende Gesellschaften* [Cross-border Corporations] (2nd edn, Carl Heymanns, Köln, 2006) § 13, para 2.

⁸⁰ For example Umwandlungsgesetz [Reorganisation of Companies Act], § 198(2).

⁸¹ cf H-F Müller, 'Internationales Gesellschaftsrecht' [Private International Company Law] in G Spindler and E Stilz (eds), *Aktiengesetz* [Stock Corporation Act] (CH Beck, München, 2007) para 12.

⁸² *Cartesio* (n 5) para 112.

⁸³ Unless it is argued that the rationale of *Centros* and *Inspire Art* requires the receiving Member State to allow conversion without re-incorporation. In this direction S. Grundmann, *Europäisches Gesellschaftsrecht* [European Company Law] (CF Müller, Heidelberg 2004) para 779; A Wiśniewski and A Opalski, 'Companies' Freedom of Establishment after the ECJ *Cartesio* Judgment' (2009) 10 EBOR 595, 615, 618.

consequence is, arguably, rather opaque and the reference in *Cartesio* to the law of the receiving Member State circular.

Case 3: The case that raises the most interesting questions is the transfer of the real seat from a real seat country (A) to another country (B) that follows either the real seat theory or the incorporation theory. It is questionable what impact articles 49, 54 TFEU (ex-articles 43, 48 EC) have on the company law of Member State A. The Court of Justice in *Cartesio* did not expressly address this question. However, the holding, when pointing out (in rather obscure English) that ‘the situation where the seat of a company incorporated under the law of one Member State is transferred to another Member State with no change as regards the law which governs that company [shall] be distinguished from the situation where a company governed by the law of one Member State moves to another Member State with an attendant change as regards the national law applicable’⁸⁴ seems to imply that our case 3 should be solved in the same way as case 2. In both cases, the applicable legal regime changes—in the first scenario through a transfer of the registered seat out of an incorporation theory State, thus altering the factor that determines the applicable law, in the second scenario through a transfer of the real seat out of a real seat State, again altering the determinative factor. Arguably, both cases should be governed by the same principles, ie in both cases the Member State of incorporation may not require the winding-up or liquidation of the company if the receiving Member State allows the change of the applicable law without re-incorporation.

Before we proceed with our argument, some terminological difficulties need to be addressed. In *Cartesio*, the Court of Justice states that ‘in the absence of a uniform Community law definition of the companies which may enjoy the right of establishment on the basis of a single *connecting factor* determining the national law applicable to a company’,⁸⁵ the Member States are free to determine when and under which conditions a company comes into existence. Thus, ‘a Member State has the power to define both the *connecting factor* required of a company if it is to be regarded as incorporated under the law of that Member State [...] and that required if the company is to be able subsequently to maintain that status.’⁸⁶ The Court concludes that a Member State may prohibit a company to transfer its seat without dissolution to another Member State, ‘thereby breaking the *connecting factor* required under the national law of the Member State of incorporation.’⁸⁷ On the other hand, the Court points out that a transfer ‘with an attendant change as regards the national law applicable’⁸⁸ falls within the scope of articles 49, 54 TFEU (ex-articles 43, 48 EC). Accordingly, measures of the Member State of incorporation that restrict this right need to be justified on grounds of an overriding requirement.⁸⁹

⁸⁴ *Cartesio* (n 5) para 111.

⁸⁶ *ibid* para 110 (emphasis added).

⁸⁸ *ibid* para 111.

⁸⁵ *ibid* para 109 (emphasis added).

⁸⁷ *ibid* para 110 (emphasis added).

⁸⁹ *ibid* para 113.

If the Court intended the words ‘connecting factor’⁹⁰ to mean the factor that determines the applicable company law (ie the connecting factor in private international law), as paragraph 109 of the judgment implies, and if it intended to use the words with the same meaning throughout the whole decision, it would manage to contradict itself within the span of three paragraphs (paras 109–111). On the one hand, a transfer of seat which breaks the connecting factor and thus changes the applicable law must be permissible without dissolution,⁹¹ on the other hand, the consequences of breaking the connecting factor fall within the power of the Member State.⁹² The only sensible interpretation is to attach two different meanings to the term ‘connecting factor’. As the Court stresses in paragraph 109, before a company can avail itself of articles 49, 54 TFEU (ex-articles 43, 48 EC), it has to be established whether the company has been formed in accordance with the law of a Member State.⁹³ This question, and the antecedent question of whose law shall govern the formation of the company, can necessarily not be predetermined by EC law.⁹⁴ Once the company has been validly formed, it may either transfer the real seat or the registered seat in a way that causes a change in the applicable law. Any national restriction in this context will be subject to freedom of establishment. Alternatively, the company may reorganize in a way that does not relate to a connecting factor for the purpose of private international law. In that case freedom of establishment does not apply. It follows from this distinction that the ‘connecting factor’ mentioned in paragraph 110 of the judgment⁹⁵ must be one that does not determine the applicable law, whereas paragraph 111 of the judgment refers to the ‘connecting factor’ in the private international law sense. Consequently, the scenario referred to in paragraph 110 of the judgment cannot be one of a company transferring its real seat out of a real seat theory State (our case 3). Rather, it must be one of a company transferring its real seat out of an incorporation theory State (our case 1).

The Advocate General has added to the obscurity by holding that Hungary followed the real seat doctrine.⁹⁶ This view is not in conformity with the interpretation of the Law on Private International Law in Hungary and common principles of conflict of laws. The provisions of the Company Act and the Law on the Commercial Register that refer to the real seat restrict the scope of application of Hungarian company law in cases that have a certain connecting factor (the location of the real seat) with another country; they do not determine the applicable law.⁹⁷ Thus, this must be the distinction that the Court of

⁹⁰ In German: Anknüpfung; French: rattachement; Dutch: aanknopping. In the translations, the ECJ again uses the same term in paras 109 and 110.

⁹¹ *Cartesio* (n 5) para 111.

⁹² *ibid* para 110.

⁹³ *ibid* para 109.

⁹⁴ Unless, as discussed above, arts 49, 54 TFEU (ex-arts 43, 48 EC) are invoked in respect to the incorporators.

⁹⁵ AG Maduro, opinion in *Cartesio* (n 32) 23.

⁹⁶ *Cartesio* (n 5) para 110.

⁹⁷ Art 18 of Decree-Law No 13 of 1979 on Private International Law Rules (a nemzetközi magánjogról szóló 1979. évi 13. törvényerejű rendelet) provides that ‘(1) The legal capacity of a legal person, its commercial status, the rights derived from its personality and the legal

Justice has in mind when it differentiates between the two situations in paragraphs 110 and 111 of the judgment in *Cartesio*. In conformity with this interpretation, the Court in *Cartesio* does not discuss the real seat or incorporation theory doctrines and, in fact, never refers to Hungary as a real seat State.⁹⁸

relationships between its members shall be determined in accordance with its personal law. (2) The personal law of a legal person shall be the law of the State in the territory of which it is registered.' Cf *Cartesio* (n 5) para 20. Para (2) of the article clearly states that the registered seat shall be the connecting factor. Thus, Hungarian private international company law is based on the incorporation theory. This connecting factor is then, for certain cases, qualified by virtue of the interplay of art 1(1) of Law No CXLIV of 1997 on Commercial Companies (a gazdasági társaságokról szóló 1997. évi CXLIV. törvény), which stipulates that the Company Act shall govern only such companies 'which have their seat in Hungary' ibid para 11, and art 16(1) of Law No CXLV of 1997 on the Commercial Register, Company Advertising and Legal Procedures in Commercial Registration Matters (a cégnyilvántartásról, a cégnyilvánosságról és a bírósági cégeljárásról szóló 1997. évi CXLV. törvény), which defines the seat of the company as 'the place where [the company's] central administration is situated' ibid para 17. The latter two provisions are not conflict of law rules. They circumscribe the scope of application of the Hungarian Companies Act by requiring a Hungarian company to have its real seat in Hungary. It can in some cases be difficult to distinguish between a provision of a purely substantive nature that contains an international element, ie that applies if a certain element is satisfied abroad or within the territory of the *lex causae*, and provisions that contain a hidden conflict of laws rule, ie that determine their international scope of application notwithstanding the *lex causae*. The second type of rule has been described as a 'self-contained' (J Kropholler, *Internationales Privatrecht* (6th edn, Mohr Siebeck, Tübingen, 2006) § 13 IV 2) or 'self-satisfied' provision of substantive law (G Kegel, 'Die selbstgerechte Sachnorm' in E Jayme et al (eds), *Gedächtnisschrift für Albert A Ehrenzweig* (CF Müller, Karlsruhe, 1976). The Hungarian provisions are not 'self-contained', they do not decide about the application of Hungarian substantive company law notwithstanding the *lex causae*. Conversely, they decide about the exclusion of that law in certain situations (when the company's real seat is not located within Hungary), which presupposes its applicability pursuant to different rules (art 18 of Decree-Law No 13 of 1979 on Private International Law Rules) in the first place.

⁹⁸ In the literature this correlation between the Court's definition of the material scope of arts 49, 54 TFEU (ex-arts 43, 48 EC) and the relevance of the term 'connecting factor' for purposes of real seat and incorporation theory often seems to be overlooked. For example, AF de Sousa, 'Company's Cross-border Transfer of Seat in the EU after *Cartesio*', Jean Monnet Working Paper 07/09, available at www.JeanMonnetProgram.org, 33, claims that 'Hungarian law apparently followed a strict version of the real seat theory.' However, had that been the case the applicable law would have changed and pursuant to paragraphs 111–113 of the judgment the Hungarian restrictions would have been within the scope of freedom of establishment. Moreover, on the basis of the bifurcation of the term 'connecting factor' suggested here the alleged 'squaring of the circle' (at 47) by the Court presents itself as a consistent distinction between the situations in paragraphs 110 and 111 of the judgment (as long as the reaction of the receiving State is not taken into account, see case 2 and case 4). In a similar vein, M Szydlo, 'Case C-210/06, CARTESIO Oktató és Szolgáltató bt, Judgment of the Grand Chamber of the Court of Justice of 16 December 2008, not yet reported' (2009) 46 CMLRev 703, explains, on the one hand, that the Court in *Cartesio* affirmed that a company's right to reincorporate in another Member State was within the scope of arts 49, 54 TFEU (ex-arts 43, 48 EC) (at 717), but alleges, on the other hand, that pursuant to *Cartesio* companies are not protected if they lose their status as a company incorporated under the law of a particular Member State because they are dissolved or a change of the applicable law takes place (at 713). A Johnston and P Syrpis, 'Regulatory competition in European Company Law after *Cartesio*' (2009) 34 ELRev 390, argue that 'any attempt by a company incorporated in a real seat Member State to move its real seat out of the jurisdiction is likely to result in the company being wound up', despite such a move resulting in an 'attendant change' in the applicable law (*Cartesio*, n 5 para 111).

Coming back to our hypothetical, seeking a consistent interpretation of the holding of the Court of Justice and placing emphasis on the words ‘an attendant change as regards the national law applicable’⁹⁹ as the defining factor in deciding whether a scenario falls within the scope of articles 49, 54 TFEU (ex-articles 43, 48 EC) or not, will lead to the conclusion that the transfer of a company’s real seat out of a real seat theory State should be treated analogously to the transfer of the registered seat out of an incorporation theory State (our case 2). Consequently, national legislation on the incorporation and winding-up of companies does not enjoy immunity from the provisions on freedom of establishment.¹⁰⁰ We must therefore look at the reaction of Member State B. If B follows the real seat theory, it will apply its internal company law. The domestic law will require registration of the company in B in order for the company to be able to convert to a company form governed by B’s law.¹⁰¹ B’s company law may or may not require re-incorporation as a

⁹⁹ *Cartesio* (n 5) para 111.

¹⁰⁰ ibid para 112.

¹⁰¹ The Court in *Cartesio* uses the term ‘conversion’ somewhat ambiguously, see eg paragraphs 111–113 of the judgment. ‘Conversion’ may be understood narrowly as the change of a company into its functional equivalent in another legal system, for example of an English limited into a German *Gesellschaft mit beschränkter Haftung* (GmbH), or broadly as any change of form of business association, for example of an English limited into a German partnership (*Gesellschaft bürgerlichen Rechts* pursuant to German Civil Code [BGB], §§ 705–740). The laws of some Member States understand conversion in the latter, broader sense, see eg Umwandlungsgesetz [Reorganisation of Companies Act], § 191(2). Such an interpretation of the Court’s decision in *Cartesio* could result in unintended liability. Assume, for example, that the directors of a limited company registered in A relocate from A to B and that both A and B apply the real seat theory. The relocation may be interpreted as the transfer of the real seat from A to B (confer the facts of *Überseering*, n 2). An unqualified application of *Cartesio* would lead to the following result: The transfer of the real seat causes a change in the applicable law. Hence, possible impediments to the transfer imposed by A are prohibited by the Treaty, provided that B allows the company to relocate and change into a form of company under its own laws. This is the case and does not require any registration or other explicit legal act by the directors of the company if the partnership law of B provides that a partnership comes into existence whenever two or more persons act together to promote the achievement of a common purpose (eg German Civil Code [BGB], § 705). Depending on the partnership law, the involuntary change of the limited company into a partnership may entail joint (or joint and several) unlimited liability of all members (eg in the UK pursuant to Partnership Act 1890, s 9, and in Germany pursuant to Commercial Code [HGB], § 128, see the decisions of the Federal Court of Justice in BGHZ 142, 315; 146, 341). Thus, rather than protect the interests of the company’s directors and members and facilitate free movement, *Cartesio* would mandate the application of unfavourable partnership law. There are two ways to avoid this result. First, note that the case described here constitutes a conflict between the holdings in *Cartesio* and *Überseering*. According to *Cartesio*, since conversion of the company into a partnership under the laws of B is permitted, A is not entitled to require liquidation ((n 5) para 111). However, a company in liquidation satisfies the requirements of *Überseering* (n 2) para 52: It is a company that has been ‘validly incorporated in one Member State (“A”) in which it has its registered office’, and it has, in this scenario, ‘moved its actual centre of administration to Member State B’. The rules governing a company in liquidation may be more advantageous for the members of the company than partnership law. Consequently, *Überseering* demands that Member State B recognises the company as a company in liquidation governed by the laws of A and that it does not apply its own partnership law. The first solution to the quandary is, therefore, to accord precedence to *Überseering* and disapply *Cartesio*. Second, the unintended consequences can be avoided by interpreting the term ‘conversion’ more restrictively and require an intentional decision of the company for conversion in order for the effects of *Cartesio* to apply

precondition for registration. If it does require re-incorporation, such a rule would be absolved from compliance with EU freedom of establishment principles pursuant to the concepts established in *Cartesio* and *Überseering*.¹⁰²

If B applies the incorporation theory, it will refer to A's law (since the registered seat of the company has remained in A). A *renvoi* (triggered by the transfer of the real seat to B) will lead to the outcome described in the preceding paragraph. Finally, let us assume that B's private international law refers to the internal (substantive) rules of A to the exclusion of its choice of law rules, or that Member State A is the forum and A's private international law accepts B's *renvoi*.¹⁰³ A's substantive company law will most likely require liquidation if the connecting factor (the real seat) is transferred out of its territory. However, *Cartesio* prohibits such a restriction in the light of freedom of establishment (save a possible justification) if (1) the transfer leads to a change in the applicable national law and (2) the transfer of the company without dissolution is permitted under the law of the receiving Member State. The law of the receiving State (B) comprises its substantive and private international law. Thus, it demands the application of A's substantive company law, which, in turn, requires dissolution. Again, we arrive at circular and nonsensical results on the basis of the concept of free movement of companies as developed by the European Court of Justice.

Case 4: A company transfers its registered seat out of a real seat theory State. This case has also not been decided in *Cartesio*. However, it is analogous to the scenario of a transfer of the real seat out of an incorporation theory State (our case 1), which are the facts of *Cartesio*. Thus, as our cases 2 and 3 demand parallel treatment, so do cases 1 and 4. It follows that the Member State of incorporation (A) can require winding-up and liquidation because the location of the registered seat in the territory of A is one of the 'connecting factors' that, according to the Court of Justice, the Member State has the power to define and that companies have to adhere to if they wish to avail themselves of freedom of establishment.¹⁰⁴ B, on the other hand, will register the company without re-incorporation if it allows for conversion into a

(see A Wiśniewski and A Opalski, 'Companies' Freedom of Establishment after the ECJ *Cartesio Judgment*' (2009) 10 EBOR 595, 615–616). This is preferable since it allows the parties to choose what is more appropriate in the individual case. At the same time, there is no reason to permit conversion (and hence the consequences of *Cartesio*) only if the host Member States provides for a functional equivalent of the home Member State company form (as A Wiśniewski and A Opalski advocate, *ibid* 616–617), as long as conversion into a non-equivalent form is consonant with the wishes of the parties concerned (see also D Zimmer and C Naendrup, 'Das *Cartesio-Urteil* des EuGH: Rück- oder Fortschritt für das internationale Gesellschaftsrecht?' (2009) Neue Juristische Wochenschrift 545, 548).

¹⁰² cf case 2.

¹⁰³ For example Einführungsgesetz zum Bürgerlichen Gesetzbuch (EGBGB) [Introductory Law to the Civil Code] art 4(1).

¹⁰⁴ *Cartesio* (n 5) para 110. Most real seat states will demand dissolution if the registered seat is transferred to another country even though the applicable law does not change: cf B Großfeld, 'Internationales Gesellschaftsrecht' [Private International Company Law] in J Kropholler et al

domestic company and if the company has not been dissolved pursuant to A's law, which is, according to B's private international law, the applicable law on this matter (notwithstanding whether B is an incorporation theory or a real seat theory State). If A does not require dissolution, it could be argued that according to the rationale of *Centros* and *Inspire Art* B likewise is not permitted to require re-incorporation or re-location of the real seat to B.¹⁰⁵

Case 5: The transfer of both the real seat and the registered seat out of a Member State that applies the incorporation theory constitutes a combination of our cases 1 and 2. Since the connecting factor between the company and the Member State of incorporation that enables the company to rely on the right of establishment (ie not—at least not only—the connecting factor within the meaning of private international law) is eliminated it might be assumed that the Member State of incorporation was entitled to require the company to dissolve.

Case 6: The transfer of both the real seat and the registered seat out of a Member State that applies the real seat theory (combination of cases 3 and 4) is treated similarly. Again, the existence of the company as a creature of the Member State of incorporation (and, therefore, the precondition for an application of articles 49, 54 TFEU (ex-articles 43, 48 EC)) hinges on the preservation of the connecting factor with the Member State of incorporation. The connecting factor (for example the real seat in the territory of the Member State of incorporation) is discontinued; therefore, the holding in *Cartesio* can be interpreted as empowering the Member State to require dissolution.

However, the treatment of cases 5 and 6 as not falling within the scope of articles 49, 54 TFEU (ex-articles 43, 48 EC) is not compelling. The connecting factor in case 1 (*Cartesio*) is the real seat, while the change of applicable law is brought about by a transfer of the registered office (case 2; also decided in *Cartesio* as being protected by the right of establishment). Nonetheless, the connecting factor that has to be satisfied for a company to be entitled to incorporate under the law of a given Member State (be it an incorporation theory or a real seat theory State) is as much the location of the real seat¹⁰⁶ as the registered seat. The company law of no country will allow incorporation as a type of company governed by that country's law without registration in the country, and hence registered seat located in the territory of the country. Why, then, should the elimination of the first connecting factor (transfer of the real seat as in case 1) allow the Member State of incorporation to impose restrictive measures, but not the elimination of the second connecting factor (transfer of the registered seat, as in case 2)? If both registered seat and real seat are

(eds), *J von Staudingers Kommentar zum Bürgerlichen Gesetzbuch* (13th edn, de Gruyter, Berlin, 1993) para 599–604.

¹⁰⁵ cf (n 83).

¹⁰⁶ Provided that the substantive company law of the Member State of incorporation is structured as Hungary's law in *Cartesio*.

transferred, as in cases 5 and 6, the applicable law changes, which, according to *Cartesio*, triggers the application of articles 49, 54 TFEU (ex-articles 43, 48 EC). This is one of the many inconsistencies of the decision of the Court of Justice.

V. CONCLUSION

This case-by-case analysis makes clear that the outcome of a free movement case under the right of establishment of companies as interpreted by the European Court of Justice depends in an arbitrary manner on the type of private international company law doctrine (real seat or incorporation theory) in force in the Member State of incorporation and the receiving Member State. Why, for example, should a company that transfers the registered seat out of an incorporation theory State (case 2) be entitled to invoke the protection of articles 49, 54 TFEU (ex-articles 43, 48 EC) whereas the Member State of incorporation may require the company to dissolve without having to fear a violation of the right of establishment if it follows the real seat theory (case 4)? The same argument can be made with respect to the differential treatment of our cases 1 (dissolution) and 3 (no dissolution). A justification for this discrimination is absent. It can probably be explained in light of the trajectories initiated by *Daily Mail* on the one hand and *Centros* on the other hand, and by the reluctance of the Court of Justice to comprehensively reform the principles established in these two cases. Ever since *Daily Mail*, the Court has adhered to the dichotomy of moving-in and moving-out scenarios and the differences in the scope of application of articles 49, 54 TFEU (ex-articles 43, 48 EC) implied by the direction of movement. In *Cartesio*, and earlier in *Lasteyrie du Sallant* and *Marks & Spencer*, the Court of Justice has retreated somewhat from a strict dichotomy. In *Cartesio*, the relaxation appears in the form of the right of a company to leave the Member State of incorporation if the transfer of seat triggers a change in the applicable company law. However, the ECJ has not yet been willing to let go of *Daily Mail* completely.

A rationalized rule governing the right of establishment should not be guided by obsolete differentiations but by the question whether free movement of companies should be facilitated. This is not a dogmatic but an empirical question. The capacity of incorporators to choose freely between a large number of company law regimes and types of company and to change the connecting factor without dissolution after the company has come into existence enables them to opt for the form and regulatory environment that best suits their needs. Consequently, it reduces transaction costs for the firm. On the other hand, the presence in the territory of a Member State of various types of company, many of them foreign and some governed by legal regimes that the domestic adjudicator is not familiar with, increases the costs of information and of legal advice for customers and other market participants and the risk of an incorrect judgment in case litigation cannot be avoided. Thus,

unrestricted free movement has a negative impact on transaction costs for third parties. A comprehensive empirical assessment of these impacts should determine whether—and to which extent—free movement of companies is desirable. Depending on the outcome of such an assessment, Member States should be allowed to restrict the transfer of companies into or out of their territory or be obliged to justify their restrictive measures in light of articles 49, 54 TFEU (ex-articles 43, 48 EC), notwithstanding whether they follow the real seat theory or the incorporation theory, whether the company has transferred the centre of administration or the registered seat, or whether a moving-in or a moving-out scenario is at issue. It is appreciated that an empirical analysis as envisaged here is complex, difficult to implement, and may not generate conclusive results.¹⁰⁷ Even so, a clarification of the convoluted legal principles is imperative in order to restore legal certainty.

¹⁰⁷ of the ambiguous results that empirical surveys in the US have produced, for example L Bebchuk et al, 'Does the Evidence Favor State Competition in Corporate Law?' (2002) 90 Cal Rev 1775, with references.