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Steps toward a Uniform Corporate Law in the European Union

Uwe Blaurock

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BERGER LECTURE

Steps Toward a Uniform Corporate Law in the European Union

Uwe Blaurock*

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* Professor, University of Freiburg.

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Introduction

Outsiders might think the European Union (EU) has grown into a homogeneous unit. However, even after the Maastricht and Amsterdam Treaties, the Union remains a loose organization of states, far from functioning as a federal entity. It does not have its own government; and the final decision-making organ, the European Council, remains an assembly composed of government representatives of sovereign member states. The member states continue to apprehensively guard their own national interests and have only handed over their right of sovereignty to the European communities in specifically delineated areas, thus creating an international organization of a very particular kind.

The central element of the European Union is the European Economic Community (EEC). The EEC was established by the Treaty of Rome in 1957 with the goal of setting up a common market for all of its member states. This common market was further developed by the Single European Act of 1986 into an "area without internal frontiers in which the free movement of goods, persons, services and capital is ensured."[1] Important as the so-called "internal market" is for the free movement of goods and services, its primary significance lies with its effect on two groups, consumers on the one hand and businesses on the other.

This Article examines the organization of businesses under corporate law in the European Union. The last thirty years have seen the development of a whole body of European regulations which have in part had a very considerable influence on the corporate law of the individual member states. These developments have obviously not come to an end, but the situation has currently reached a point that allows one to take stock of developments and to see the changes that have already taken place in individual corporate laws, and more particularly to examine the changes that are yet required.

I. Why Is the Harmonization of Corporate Law in Europe Necessary?

A. What is European Corporate Law?

In its White Paper entitled *Completing the Internal Market*, the Commission, as a part of the structuring of a single European market, set the task of creating a suitable legal framework in the field of corporate law for the facilitation of cross-border cooperation and activities.[2] Today, this goal of achieving a fully operational unified legal framework still has not been completely realized. On the one hand, "European corporate law" is therefore the sum of all Community regulations in the field of corporate law currently in force and, on the other hand, it is a legislative program.

1. Treaty Establishing the European Community, Feb. 7, 1992, 1992 O.J. (C 224) 7a [1992] 1 C.M.L.R. 573 [hereinafter EC Treaty].

2. Commission of the European Communities, Completing the Internal Market: White Paper from the Commission to the European Council 35 (1985).

B. Market Freedoms

The bases for achieving an internal market are the basic freedoms set out in the EC Treaty. These are the free movement of goods,[3] the free movement of persons[4] and the free movement of payments and capital.[5] The most important freedoms for corporations are the free movement of persons, the freedom of establishment[6] and the freedom to provide services.[7]

1. Freedom of Establishment

The freedom of establishment guarantees the general right to create permanent institutions necessary for the independent operation of business activities and, in particular, the right to set up corporations.[8]

Freedom of establishment really only exists when the legal personality of a corporation in a particular state is also recognized in other member states. The legal capacity of a corporation is defined in its memorandum and articles of association. Precise delineation of what exactly these comprise is, however, problematic. In Europe, this issue is at present regulated in two different ways, depending on the legal concepts applied.

The first of these concepts focuses on the initial step of foundation, or formation. Under the *foundation theory*, the articles of association are subject to the laws of the state in which the corporation is established. If a corporation is established in accordance with the laws of the state in which it is established, its legality should, according to this theory, also be recognized by other states in which the corporation operates. Its status as a legally operating entity should also be recognized if the corporation has "emigrated" to another state.

In contrast, the second concept emphasizes the relevance of the seat of a corporation. The *place of registration theory* demands that a corporation be incorporated in accordance with the laws of the state in which the actual administrative center of the corporation exists, or the location of the decision-making center of the corporation. This emphasis on the place of registration has the effect of restricting the freedom of movement of corporations.

Because various member states within the EU have taken different positions on the recognition of international norms relating to corporate law, corporations in the EU face potentially conflicting conditions with respect to their freedom of movement, depending on the state in which the corporation was established and the state to which it intends to relocate. I will return to this point at a later stage.

3. EC Treaty arts. 9-36.
4. *Id.* arts. 48-66.
5. *Id.* arts. 67-73(h).
6. *Id.* arts. 52-58.
7. *Id.* arts. 59-66.
8. *Id.* art. 52(2).

2. *Competitive Equality for Persons Operating in the Common Market*

From a corporation's point of view, corporate laws regulating liability necessitate the use of services (such as auditing and notarization) that require the establishment of certain corporate organs or the deployment of certain personnel. As a result, these corporate laws amount to operational cost factors. In this sense, they are important "location factors." Understandably, no goals have been set to create identical location conditions throughout the European Union in relation to financial matters such as the costs of real estate, transport or other comparable economic factors. If, however, differences arise that are not only attributable to local conditions or to a state's tax regime, but also to different corporate law regulations for what are essentially the same economic facts, this can result in an inequality in competition conditions for businesses. This is not compatible with article 7a of the EC Treaty,[9] which calls for the creation of an economic area without internal frontiers.

C. Competing legal systems?

One can ask, however, whether it is really necessary for the creation of an internal market to harmonize national corporate laws and create supranational corporate structures. Perhaps European legal harmonization diminishes the benefits of competition between the different legal systems. Competition between legal systems may ascertain, over time, which system proves to be the most sensible and practical. The American system illustrates such competition. There are fifty different legal systems in the United States, and difficulties seldom arise when working between the different corporate laws. The uniform U.S. market allows different legal systems to coexist without suffering from the results.

There are, however, major differences between the United States and the European Union that must be taken into account when considering this question. Apart from the special case of Louisiana, the legal systems of the individual states in the United States have their shared basis in the common law. They share a similar legal culture, and legal training in individual states is almost identical. Despite differences in finer details, corporate law is therefore quite similar. Moreover, some sections of the law regulating capital markets are under federal control and apply to all states in the same way.

The situation in the European Union is entirely different. The legal systems of the member states belong to different families of law. Some legal systems are based on common law and others on civil law. In the civil law systems, both the Roman and Germanic legal traditions are represented. And until recently, there were absolutely no Europe-wide regulations concerning capital markets.

For this reason, the conditions for a healthy competition of legal systems did not exist in Europe in the area of corporate law, and they still do not today. Furthermore, as mentioned already, the member states of the

9. EC Treaty art. 7a.

European Union follow different models when dealing with conflicts of corporate law regimes. Some states adhere to the place of registration theory, and others base their law on the foundation theory. Businesses wishing to operate in states where the place of registration theory applies must take all the advantages and disadvantages of the *local* legal system into consideration when deciding on the issue of location.[10] Businesses can only operate under a legal regime other than the one applicable in their state of location in which they are located if the foundation theory applies. As far as I am aware, all of the U.S. states follow the foundation theory, and this fact alone shows clearly the fundamental differences between the United States and the European Union.

In addition, one of the substantial weaknesses of competition between corporate law systems is that it may attract a member state to follow a policy of systematic corporate law deregulation with the goal of attracting as many businesses as possible to that country.[11] In Europe, this phenomenon has been labeled the "Delaware Effect" due to similar developments that have taken place in the United States. Systematic deregulation risks a decrease in the quality of corporate law, particularly with respect to the protection of creditors and minority shareholders. In contrast to the United States, this danger has not yet been contained in Europe by enabling adequate protective regulations in the laws governing the capital markets and stock exchange transactions.

Unrestricted competition between the various systems of corporate law is for these reasons not the right answer for Europe. A controlled harmonization of corporate laws with the aim of making corporate law a *neutral competitive factor* in the decision of corporate location would appear to be the more sensible way forward.

II. Forms of Harmonization of Corporate Law in the EU

Harmonization has always been the goal of the European Commission, which has endeavored to create a legal framework for corporations operating in a single market that facilitates cooperation and business activity. Its efforts have concentrated on four main areas:

(1) harmonization of national corporate law regimes with respect to content;
(2) mutual recognition of national corporations in the individual member states of the European Union;
(3) creation of the legal possibility for national corporations of merging with corporations from other European countries and of transferring their seat from one country to another and ensuring that the conditions

10. Wolfgang Schön, *Mindestharmonisierung im europäischen Gesellschaftsrecht*, 160 ZHR (Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht) 220, 235 (1996).

11. Hanno Merkt, *Das Europäische Gesellschaftsrecht und die Idee des "Wettbewerbs der Gesetzgeber,"* 59 RabelsZ (Rabels Zeitschrift für ausländisches und internationales Privatrecht) 545, 549 ff. (1995).

under which these steps are possible are practical – also from a taxation point of view;
(4) creation of forms of supranational corporations.

The EC Treaty offers three ways to standardize or harmonize laws: agreements under article 220 of the EC Treaty, regulations, and directives. Brief explanations of each follow.

Under article 220 of the EC Treaty, *agreements* are international law agreements that are signed by individual member states and that supersede any opposing national law; the rules entailed address the individual citizens of states ratifying the agreement. Under article 189(2) of the EC Treaty, *regulations* are generally and directly applicable in all member states. They are enacted by the Council. Regulations are binding on citizens of all of the member states of the European Community. A European regulation takes priority over national law. *Directives*, also enacted by the Council, are directed at national legislatures of member states. They require the legislatures to implement their contents into national law by passing appropriate legislation. The legislature has some flexibility in the choice of form and methods for implementation of the goals described in the directive. A directive is thereby a flexible rule that has no binding effect in total, only the goal to be achieved is binding.[12] A directive gives member states a degree of flexibility when embedding its goals into their national legislation, allowing them to take the requirements of their own particular legal systems and their own legal terminology into consideration.[13] Each of these three forms of European legislation arise in the area of corporate law, though in varying degrees of frequency. *Agreements* do not play a role in European corporate law. To date, there has only been one agreement, which was made in 1968 and deals with the mutual recognition of corporations and legal persons within the EU.[14] However, not enough member states have ratified the agreement, so that it can now be considered to be obsolete.[15] *Regulations*, legal acts with direct application in the entire area of the European Union, are of greater importance. I shall come back to elaborate on this point in a moment.

The vast majority of Community legislative measures in the area of corporate law are *directives*, legal acts directed at member states binding them to implement the contents into national law. Directives are at the core of the legal framework for a Europe-wide harmonization of corporate law. They are based on the special rules found in article 54(3)(g) and article

12. Hans-Wolfram Daig, *Gemeinsame Vorschriften für mehrere Organe*, *in* 2 KOMMENTAR ZUM EWG-VERTRAG: ARTIHEL 137-248 536-87, 551 (Groeben et al. eds., 1983). Gudrun Schmidt, *Gemeinsame Vorschriften für mehrere Organe*, *in* 4 KOMMENTAR ZUM EU/EG-VERTRAG art. 189 Rn. 24, 36-38 (Hans von der Groeben et al. eds., 1997).

13. Christiaan W. Timmermans, *Die europäische Rechtsangleichung in Gesellschaftsrecht*, 48 RABELSZ (RABELS ZEITSCHRIFT FÜR AUSLÄNDISCHES UND INTERNATIONALES PRIVATRECHT) 1, 10 (1984).

14. BGBL. II (BUNDESGESETZBLATT TEIL II) 370 (1972).

15. Dauses/Behrens, HANDBUCH DES EG-WIRTSCHAFTSRECHTS E.III at 116 (Manfred A. Dauses ed., 1988 ss).

57(2)(1) of the EC Treaty and the general rules of articles 100-102 of the EC Treaty.

Article 54(3)(G) of the EC Treaty states:

> The Council and the Commission shall carry out the duties devolving upon them . . . by coordinating to the necessary extent the safeguards which, for the protection of the interests of members and others, are required by Member States of corporations or firms . . . with a view to making such safeguards equivalent throughout the Community.

The wording "*necessary extent*" is of particular importance in this context.

To date, fourteen directives and proposals for directives have dealt with the harmonization of substantive corporate law in the member states of the European Union. Nine directives have already been enacted, and five are still in the preparatory stages, as preliminary drafts.[16] The directives already enacted deal with the rules of public disclosure, the foundation of corporations, the protection of capital in corporate provisions, representative authority of managerial bodies, the submission of accounts (including accounts for final audits), and corporate mergers and divestitures (splits). The laws regulating the certification of incorporation of stock corporations, the responsibilities of corporate organs, codetermination (representation of labor on a corporation's supervisory board), and groups of corporations are examples of areas that still must be addressed.

III. European and National Law

European legislation has clearly changed national corporate law in many areas, particularly thanks to the harmonization measures that have altered the corporate law of member states. Work is in progress to create new forms of supranational corporations that will give corporations operating on a Europe-wide basis a standardized organizational framework. Because these new corporate forms will be introduced under a uniform law, regulations enacted by the Commission are the most appropriate instrument to effect this change.

A. Standardized Corporate Forms in Europe

There has been one successful project to date in relation to the creation of uniform corporate forms within Europe; however, several other projects have not been successful.

1. *European Economic Interest Groupings (EEIG)*

The only Europe-wide uniform corporate form that currently exists is the European Economic Interest Groupings (EEIG). It is an instrument for cooperation and serves to support the economic activities of its members.

16. Peter M. Wiesner, *Stand des Europäischen Unternehmensrechts*, 6 EuZW (Europäische Zeitschrift für Wirtschaftsrecht) 821, 824 (1995); Dauses/Behrens, *supra* note 15, at 18.

In this respect, it carries features of a cooperative[17] and is based on the model of the French *groupement d'interêt économique.* The EEIG Regulation only covers the legal *frame*, which is then supplemented by national law. In Germany, for example, this supplementary function is performed by the Implementary Act for the EEIG Regulation and, subsidiarily, the provisions relating to General Partnerships (the so-called "OHG") contained in the Commercial Code. The legal rules to be applied in Germany are, thus, found in four different sources of law: The EEIG Regulation, the Implementary Act for the EEIG Regulation, the Commercial Code, and the Civil Code, which contains the basic rules governing partnerships. Thus, application of the EEIG Regulation is not made particularly easy.

The EEIG corporate form deliberately does not address several critical areas that have so far proved an obstacle to agreement on the creation of a European Stock Corporation. This affects, in particular, the issue of codetermination. The upper limit for the number of employees in an EEIG is 500, thus avoiding the whole question of codetermination, which only arises in larger corporate entities.

The EEIG is gaining popularity in the European Union.[18] It is especially favored by self-employed persons for cross-border cooperation.

2. *European Stock Corporation*

The European Stock Corporation – *Societas Europaea* (SE) – has, so far, met with little success. This is the oldest project directed at creating a standardized corporate form in Europe for cross-border business operations.

After preliminary considerations beginning in 1959, the Commission produced the first draft for a statute of a European Stock Corporation in 1970. A second draft followed in 1975. Both drafts regulated in detail the administrative structure of the SE, the rules of codetermination, the law in relation to group corporations, the law regulating the accounting of an SE and even several points concerning taxation. The 1975 draft, however, was rejected by the Council of Ministers. The Commission presented a completely new draft in 1989 that was clearly different from both of its previous submissions. In this new effort, the Commission moved away from the idea of creating a purely supranational legal form unaffected by national regulations, and instead the draft included many references to national law. At this stage, it was much easier to give national laws a role than it had been in the previous drafts dating back to 1970 and 1975, because a much higher degree of harmonization had been achieved since the first drafting attempts. The draft statute was divided into the actual *statute* of the SE (article 100 of the EC Treaty being the legal basis) and a draft *directive* for codetermination (article 54 of the EC Treaty). The Commission

17. Jens Rinze, *Die Europäische Wirtschaftliche Interessenvereinigung – eine genossenschaftliche Rechtsform europäischen Rechts, in* AKTUELLE PROBLEME DER GENOSSENSCHAFTEN 111 (Bernd Jöstingmeier ed., 1994).

18. In the beginning of 1997 there have been 722 EEIG in Europe. *See* Hans-Werner Neye, *Neue europäische Initiative in Gesellschaftsrecht*, GMBHR (GMBH-RUNDSCHAU) R 97 (1997).

tried in this way to avoid the procedural requirement that the Council adopt *regulations* by unanimous votes.[19]

In 1991, the Commission presented a modified proposal. The technique of making use of cross-references to national laws characteristic of the 1989 draft was further developed, and independent rules were further reduced. The division into an actual draft statute and a directive on codetermination was retained. With regard to corporate structure, member states are free to opt for either the monist or dualist model. No less than four options are available for codetermination. In the 1991 draft, regulations governing corporation groups were completely dropped.

The 1991 draft was also unsuccessful. Due to the very different opinions on codetermination, all drafts to date have failed. For some time it appeared that the Commission had given up all plans with resignation, but adoption of the "Euro Staff Committee Directive"[20] has provided a new impulse. In a statement issued in November 1995, the Commission developed new options for the SE in which codetermination is separated from the legally defined organizational structure of the corporation and replaced by an information and consultation procedure along the lines developed by the Euro Staff Committee Directive.[21] Reactions in Germany to this approach have, however, not been very positive.[22]

3. *Further Suggestions Made in 1992*

In 1992, the Commission presented three further proposals based on article 100a of the EC Treaty for regulations pertaining to uniform European corporation forms. *European Associations*, *European Cooperatives*, and the *European Mutual Corporations* all came under consideration. When and in what form these entities will emerge as legally available options remains open.

B. Harmonization of National Law

Of clearly greater importance to national legal systems than the endeavor to establish supranational corporation forms are the directives leading to noticeable reforms in several areas of corporate law. This section discusses the main points involved.

1. *Public Disclosure*

Public disclosure is an area that the Commission tackled at an early stage. A large number of directives exist in this area, the main policy goal of which is to secure third party protection and create contractual certainty

19. EC Treaty art. 235.

20. ABl. EG (Amtsblatt der Europäischen Gemeinschaften) No. L 254 from 30.9.1994, at 64.

21. *Cf.* Martina R. Deckert, *Europäisches Gesellschaftsrecht – Eine Zwischenbilanz*, 35 DStR (Deutsches Steuerrecht) 874, 878 (1997).

22. Walter Kolvenbach, *Neue Initiative zur Weiterentwicklung des Europäischen Gesellschaftsrechts?*, 7 EuZW 229, 232 (1996); Peter Behrens, *Krisensymplome in der Gesellschaftrechtsangleichung*, 7 EuZW 193 (1996).

within the Union. The parties to a contract involving a corporation operating within the EU should not be confronted with unexpected surprises in relation to, for example, the legal legitimacy of a corporation's existence, the validity of the obligations agreed to by the corporation, its creditworthiness, the extent of security provided by its share capital, or the reliability of the annual financial report. As early as 1968, the rules of public disclosure as a means of achieving third party protection were, to a certain extent, the subject of the first directive on corporate law.[23] They prescribe the introduction of publicly accessible registers and the publication of certain data in official notifications for all member states. They set out the documents to be submitted to these registers as well as the ways in which third parties are affected by publication. These rules related to the formalities of public disclosure are supplemented by directives regulating the substantive aspects of public disclosure,[24] including the methods used to prepare and the contents of a corporation's or a group's annual report.[25] These directives on the substantive aspects of public disclosure are linked with the directive dealing with the qualification requirements for annual report auditors,[26] forming a compact system that has been implemented into German law by the Accounting Directives Law, enacted in 1985.[27]

The area of internal disclosure is covered by the Directive on the Duties of Disclosure on Acquisition of Shareholdings of 1988,[28] known as transparency directive. German stock corporation law stipulates that there is a duty to disclose in the case of shareholding acquisitions of 25% and 50%. The transparency directive considerably extends this duty by requiring disclosure in the event of shareholdings of 10%. Further transparency directive threshold values are 25%, 50% and 75%. In contrast to the German stock corporation law, however, this directive only affects corporations listed on the stock exchange. The directive was implemented into German law in the Securities Trading Law of 1994.[29]

2. *Internal Structure of Corporations*

In addition to the establishment of uniform rules for public disclosure, regulations affecting the internal structure of corporations and their public appearance have an important impact on the fabric of the uniform market. Those dealing with corporations outside of their own country must know how and with whom they can make contractual agreements. In a common

23. ABl. EG No. L 65 from 14.3.1968, at 8 fl.

24. Karl Gleichmann, *Überblick über neue Kooperationsformen und über Entwicklungen im Gesellschaftsrecht der Europäischen Wirtschaftsgemeinschaft*, 33 AG (DIE AKTIENGESELLSCHAFT) 159, 160 (1988).

25. 4. directive, ABl. EG (AMTSBLATT DER EUROPÄISCHEN GEMEINSCHAFTEN) No. C 7 from 28.2.72., at 11 ff. and 7. directive, ABl. EG No. L 193 from 18.7.1983, at 1 fl.

26. 8. directive, ABl. EG No. L 126 from 12.5.84, at 20.

27. BIRILIG (BILANZRICHTLINIE-GESETZ) from 9.12.1985, BGBl. I (BUNDESGESETZBLATT TEIL I) 2355 (1985).

28. ABl. EG (AMTSBLATT DER EUROPÄISCHEN GEMEINSCHAFTEN) No. L 348 from 17.12.1988, at 81 fl.

29. Securities Trading Law of 1994, §§ 21 ff. WpHG.

market, the regulations on these issues must work in a homogeneous manner. The very first corporate law directive, enacted in 1968,[30] provided this kind of certainty among contracting parties by recommending homogeneous standards for the definition of legal representation. As a result, limitations on the powers of representation of executive management, acting outside of the corporate purpose, and the failure to fulfill required formalities when establishing a corporation, among others, are defenses available against the claims of a third party in only very limited, exceptional cases.

The structure of corporations is also affected by the Directives on the Transformation of Corporations of 1978[31] (the Third Corporation Directive) and the Directive on Splitting of 1982[32] (the Sixth Corporation Directive). Whereas the First and Second Corporation Directives were strongly influenced by German corporate law, the directive dealing with mergers and splits was primarily based on Roman law, and particularly on French law models.[33] Both aim at providing earlier protection for shareholders by requiring an independent examination of intended mergers or splits. Employee interests, in contrast, receive only very low-priority consideration. Germany made use of the opportunity presented by these directives to completely revise its largely outdated law in this field and passed the Law Regulating Transformation of Corporations in 1994.[34]

Finally, the Second Corporation Directive is relevant to the internal structure of corporations. It stipulates that state corporations must have a uniform minimum level of capital resources and contains numerous provisions that serve to ensure that the initial capital required when establishing the corporation, and any later capital increases are in fact paid and that the capital is actually received.[35] This directive is in force, though only four of the member states, among them Germany (since 1979),[36] have to date implemented it in national law. Breach of Treaty proceedings are currently being taken against the remaining member states.[37]

3. *Protection of Investors*

A third area where harmonization of the law is necessary for a uniform internal market is the protection afforded to investors. If corporations are placed in a position to access equally the capital markets throughout Europe, then the acquisition modalities laid down in the stock exchange law and the regulations protecting future shareholders must offer the same qualities throughout the Union. This has been accomplished by the Direc-

30. ABl. EG No. L 65 from 14.3.1968, at 8 fl.
31. ABl. EG No. L 295 from 20.10.1978, at 36 fl.
32. ABl. EG No. L 378 from 31.12.1982, at 47 fl.
33. See also the reasons for the Verschmelzungsrichlinie-Gesetz, BT-DRS. (DRUCKSACHE DES DEUTSCHEN BUNDESTAGES) 9/1065, at 13.
34. From 28.10.1994, BGBL. I (BUNDESGESETZBLATT TEIL I) 3210 (1994).
35. ABl. EG (AMTSBLATT DER EUROPÄISCHEN GEMEINSCHAFTEN) No. L 26 from 31.1.1977, at 1 fl.
36. BGBl. II (BUNDESGESETZBLATT TEIL II) 1959 (1978).
37. Gleichmann, *supra* note 28, at 161.

tive on Admission of Securities to the Stock Exchange of 1979,[38] the Directive on Prospectuses of 1980,[39] and the Directive on Semi-Annual Reports of 1982.[40] In addition, several proposals have been submitted to the Commission dealing with subjects such as the question of issuing prospectuses, the problems related to insider information and takeover offers, an area of growing importance in Europe.

The main functions of the law governing transactions in capital markets are, of course, to ensure that the capital markets work efficiently and to protect individual investors. Creditors are only protected to a very limited degree and minority shareholders essentially enjoy no protection. Corporate law is far more suitable to deal with these issues. Within Europe, there are, however, two fundamentally different approaches in this context. On the continent, the interests protected by corporate law play a dominant role, whereas in Great Britain, as in the United States, the interests of capital markets are given priority. A look at the economic situation in the two regions quickly explains this contrast. In Germany, only 14.6% of all households own shares. This figure is 29.6% in Great Britain. Market capitalization as a percentage of gross domestic product in Germany is 18.23%; in Great Britain it is 88.55%. Assuming that no significant short-term changes alter these proportions, one can safely assert that there will be no shift in Germany in the protection of investment capital from the domain of corporate law to the laws regulating the capital market. A further limitation in the scope of capital market law is that investor protection only exists for publicly offered assets, and it is restricted to shares in public corporations. The whole area of partnerships and limited liability corporations, particularly important in Germany, is only accounted for in a very inadequate way.

4. *Partnership Law*

The law governing partnerships has been largely excluded from European harmonization. This applies to both the harmonization efforts made by the European Commission and the spontaneous steps toward harmonization taken by courts and practitioners in the member states. In addition, wherever attempts have been made, the results were, at best, ambivalent. Harmonization in this field of law makes sense in order to avoid the effective exclusion of smaller and medium enterprises from the benefits of the single market. In Germany those enterprises are mostly organized as partnerships. It can only be hoped that the Commission takes a closer look at this area in the future.

38. ABl. EG (AMTSBLATT DER EUROPÄISCHEN GEMEINSCHAFTEN) No. L 66 from 16.3.1979, at 21 ff.
39. ABl. EG No. L 100 from 17.4.1980, at 1 ff.
40. ABl. EG No. L 48 from 20.2.1982, at 26 ff.

IV. Interim Balance Sheet

An overview of corporate law in all of the EU member states reveals that the activities of the European Community and the spontaneous harmonization of laws between individual member states have already resulted in an impressive degree of legal harmonization. However, there are still marked differences in many important areas of the various national corporate laws throughout the EU.

A. Harmony in the Corporate Law of the EU States

Several areas of correlation exist among the national corporate laws of EU states. These include:

- The rules governing nominal, or stated, capital and its function as a security for creditors are now largely the same throughout Europe. This is actually a remarkable achievement when we consider the fact that the concept of fixed share capital, an idea which has prevailed in continental law for over 100 years, did not exist at all in Great Britain. As a result, very fundamental changes have taken place in English law.
- The rules for rendering accounts, at least in so far as they pertain to the protection of creditors and seek to prevent false disclosure of profits, are now more or less the same in all member states. This also holds true for the examination of annual financial statements and their public disclosure.
- The powers of representation of executive management are almost identically defined in the member states. Again here, the changes made in English law, which followed the ultra vires principle, were particularly far-reaching.
- The possibilities for merging and splitting corporations, vital elements of entrepreneurial life, are also regulated in a comparable way throughout the Union. In Germany, this meant a complete revision of the law of transforming corporations.
- Finally, corporate law now permits single person corporations, and the establishment of single person corporations is now to be ubiquitously introduced in all member states. It should be noted that this directive has not yet been implemented throughout Europe.

B. Differences Between National Laws

The remaining differences concern fundamental issues of corporate law, making harmonization in these areas particularly difficult, requiring that each member state carefully reviews its own position on the matters in question. Presently, the following four areas are under consideration: 1) the administration of stock corporations; 2) codetermination; 3) corporate law relating to groups; and 4) international corporate law.

1. *Administration of Stock Corporations*

Within the European Union, there are various models for the administration of stock corporations. The dualistic system – based on an executive board of management and a supervisory board of directors – is found in Austria, Denmark, Finland, Germany, the Netherlands, Portugal, and Swe-

den. The monistic system — based on a single corporate directive organ — prevails in Greece, Ireland, Italy, Spain and the United Kingdom. France introduced an optional model in 1966 and again in 1994 whereby there is a choice available between the monistic system, its dualistic counterpart, or the *Sociétè par actions simplifiée*, which offers a model more or less free of contractual requirements.

A draft directive on corporate structure would attempt to harmonize the articles of national stock corporations accross Europe by allowing these corporations to choose between several options. Both the monistic and the dualistic models are offered by the draft directive to structure the organs of a corporation. The dualistic model then offers four separate variations for the organization of codetermination, and three variations available under the monistic model. I have serious doubts as to whether this variety of choices really will bring about an equality of regulations.

2. *Codetermination*

The second area concerns the codetermination rights of employees. There are extremely large differences of approach on this point within the EU. In some countries, entrepreneurial employee codetermination in stock corporations is an integral part of corporate law. This phenomenon exists in Austria, Germany, Luxembourg and the Netherlands, though the regulations vary greatly even within these countries. In France, Ireland, and Portugal, partial aspects of codetermination are regulated by law. In Great Britain, Italy, Spain, and Sweden, there are no regulations, although many voluntary codetermination models exist in practice. In Belgium and Greece, codetermination is not practiced at all.

Codetermination is practiced most extensively in Germany. Corporate law prescribes a one-third parity or half parity codetermination relationship, depending on the number of persons employed in the corporation. Only businesses with less than 500 employees are exempted by corporate law from practicing codetermination. However, in addition to the codetermination prescribed by corporate law, primarily involving participation at corporation supervisory board level, the Works Constitution Law provides for an internal right of workers to both participate in the decision-making process of the business and lodge complaints. This law even affects comparatively small corporations.

With its wide range of options, the draft guideline on corporation structures does not offer the prospect of accomplishing a harmonization in this field, but, if passed, risks creating the illusion of harmonization.[41] In Germany, there are fears that corporations might "flee from the constraints of codetermination;" Great Britain objects to the concept of setting the rules of codetermination by law and considers this to contradict the long tradition of relationships between workers and the representatives of capital. And indeed, the optional models offered in the most recent draft for

41. Klaus J. Hopt, *Harmonisierung im europäischen Gesellschaftsrecht*, 21 ZGR (ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT) 265, 279 (1992).

the Statute of an European Stock Corporation read like a capitulation given that the goal is to harmonize the existing differences in approach.

3. *Corporate Law Relating to Groups*

Clear differences also exist in the corporate laws relating to groups. Legislation regulating this area has been passed, to date, only in Germany and Portugal. Belgium also recently adopted legislation that covers some aspects of the issues involved. A draft directive on the law relating to groups has been on the table since 1984. However, it has not yet found majority support within the Commission. In most member states, protection is afforded by the relevant regulations governing the capital market. The disadvantage here, however, is that these only apply to corporations traded on the stock exchange, or to publicly available shareholdings. Protection mechanisms relating to liability have been developed by judge-made law, particularly in England and France.

Germany is one of the legal pioneers in the field of business combination law, and for a long time it was believed that it would develop into a legal export article. This has not occurred. The reason why a standardization of the law relating to group businesses has not taken hold is due to fundamental differences in understanding among the various member states, and this should give cause for Germany to reconsider its position on the issues involved.

The law relating to groups in Germany is based on the fiction that a business taking part in a group is independent. This independence can only be restricted in the ways laid down in the law relating to groups, and these assume a balancing out of any disadvantages incurred through restriction. The concept envisages that such compensation is primarily regulated in a contract between the corporations involved, which outlines in a transparent manner any existing relationship of dependency. However, the functioning of real groups without a contractual basis makes it very clear that the concept of independence upon which the law is based is, indeed, a fiction. The prime interest of a group, its perspective of the entire operations and not only of individual parts, gets lost in the German focus on protecting minority shareholders and creditors.

The German system, based as it is on a group contract, is unique. In most EU member states, the concept of prescribing a *contractual* relationship to regulate the relationship of the corporation to the group is considered to be an unnecessary prescription that is, in its very nature, foreign to the business possibilities available to a group.[42] The liability system in German law is also predominantly considered to be too rigid in the other countries of the EU. In comparison, French law more readily takes account of managerial breaches of duties of conduct. A majority shareholder who exerts influence on the management organs of a dependent

42. Yves Guyon, *Examens critiques des projets européens en matière de groupes de sociétés (le point de vue français)*, *in* GROUPS OF COMPANIES IN EUROPEAN LAWS 155, 164 (Klaus J. Hopt ed., 1982).

corporation is liable as *dirgeant de fait* to compensate for any excessive debt incurred due to the influence of that shareholder.[43] Legal transactions conducted jointly by parent and daughter corporations (*unité en apparence*) can give rise to liability under the principles of prima facie entitlement.[44] Similar rules are found in English law.

4. International Corporate Law

The area of law concerned with groups is closely related to international corporate law. The beginning of this Article referred to the existence of several opposing theories relating to the question of recognition of corporations. These theories have particular significance in relation to the transfer of a corporation's principal place of business across borders.

The *foundation theory* is based on the assumption that a corporation formed according to the laws of a state will be recognized as a body possessing legal personality for the entire duration of its existence and that it will still be recognized as such even if it moves its registered place of business out of the state in which it was founded. If all states in the European Union followed the *foundation theory*, corporations would be free to move without restrictions within the Union (except in relation to taxation rules). However, under *place of registration* regimes, corporations must fulfill the requirements for registration of the state in which the principal place of business is located. If the law in all states in the Union were based on the *place of registration theory*, then it would no longer be possible to speak of the freedom of movement for corporations, because corporations transferring their place of business across borders would have to re-establish themselves in their new location. Yet, each theory has a number of adherents in the EU. The *foundation theory* is practiced in various forms in Denmark, Great Britain, Ireland, Italy, the Netherlands, Sweden, and, in a restricted form, in Spain. The *place of registration theory* is practiced in Germany, Austria, Belgium, France, Greece, and Luxembourg.

The arguments supporting the *place of registration theory* can be reduced to one point: corporations that have not fulfilled the requirements for establishment in a state should be prevented from becoming operative in that state; regulations concerning the establishment and administration of corporations in other states are not considered to be of equal value to the state's own national laws. In relation to non-EU states, this concern regarding the place of registration may be justified. Yet, the situation within the European Union is different. Corporate laws in the Union have now become so similar in so many areas that one can safely assume that the laws regulating the establishment and administration of corporations are of *equal value*.

43. Jean Nicolas Druey, *Das deutsche Konzernrecht aus der Sicht des übrigen Europa*, *in* KONZERNRECHT IM AUSLAND 310, 319 (Marcus Lutter ed., 1994).

44. Yves Guyon, *Das Recht der Gesellschaftergruppe in Frankreich*, *in id.* at 76, 90; Druey, *supra* note 47, at 317; Frank Woolridge, *Aspects of the Regulation of Groups of Companies in European Laws*, *in* EUROPEAN COMPANY LAWS: A COMPARATIVE APPROACH 103, 116 (Robert R. Drury & Peter G. Xuereb eds., 1991).

Harmonization of the rules for regulating the conflict of corporate laws in line with the *foundation theory* is necessary within the European Union. As previously explained, several basic differences concerning corporate law exist, and they are currently preventing consensus on the matter in Europe. The transfer from the *place of registration theory* to the *foundation theory*, therefore, could be qualified in the following way: as long as the basic differences exist, the receiving states must take these differences into account in the case of a cross-border transfer of the place of registration. This primarily concerns the issue of codetermination. Until laws are harmonized, the imperative regulations of each state of the (new) location must prevail. This forms the subject-matter of the so-called "*overlapping theory*," which is a modification of the foundation theory. For example, if an English public limited company transfers its place of registration to Germany, then it should be immediately recognized as a corporate body; its English internal organization should also be recognized. However, as far as codetermination laws are concerned, the statute of the organization of the corporation – its Memorandum of Association – must conform to German regulations. Re-establishment would then be no longer necessary on a transfer of its place of registration. Only corresponding modification of its statute is required.[45]

Conclusion

Corporate law in Europe is heading down the right path. If a truly uniform internal market is to be achieved, a framework of laws for the organization of businesses that has a neutral impact on their competitive situation must be created. A high degree of standardization of laws has already been achieved in the area of corporate law in the European Union. The differences that remain are based on different national attitudes and the political consensus that prevails in the individual states. The path to a fully uniform market is becoming increasingly steep and rocky. In order to tackle the next steps, all of the European states must rid themselves of some of the weight they continue to carry around with them. This is difficult and requires a high level of willingness to compromise. I, however, trust in the ability of lawyers and politicians to reason, and I am confident that we will achieve a truly *European* corporate law in the future.

45. This closely corresponds with the Spanish practice of law.