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GUEST EDITORIAL: FIRST STEPS FOR A EUROPEAN LAW ON CORPORATE GROUPS

1. Introduction

In Europe, the laws relating to business enterprises – and company law in particular – are national laws; the harmonization measures within the European Union have not changed that. However, as has been known for a long time, this leads to severe impediments in the common market: enterprises cannot transfer their seat across a border or engage in a cross-border merger. If they try to do so nevertheless, it will result in the emergence of companies of national law only. Despite these difficulties, the most important undertaking of the European law of enterprises – the Societas Europea – has just failed once again.[1]

Since usual measures for restructuring enterprises which cross borders are not feasible, more and more complicated corporate groups come into being. But they are also subject only to national laws. Germany, Portugal and Austria allow the possibility of a corporate group that is connected by means of a contract; in other European Union Member States, this legal construction does not exist. Therefore, this elegant way of bringing about a "cross-border quasi-merger" is more or less impossible in Europe. Moreover, the various Member States have different rules governing the relation between the parent company and the subsidiary, especially as regards the degree to which the parent may influence the subsidiary's management and the restrictions on this influence. A Danish parent company and its management can only learn at great cost and with great risks what "directions" it can give to its subsidiaries in Palermo, Barcelona and Birmingham without incurring its own liability for the subsidiary and its debts. In other words: the existence of different national laws on corporate groups causes a substantial hindrance to enterprises in the common market.

1. In early December 1998, the Council of Ministers intended to vote on the third altered proposal for a statute for the Societas Europea. The project failed due to objections by various Member States, notably Spain. See also Kolvenbach, "Scheitert die Europa-AG an der Mitbestimmung?", 15 *Neue Zeitschrift für Arbeitsrecht* (NZA) (1998), 1323, 1328.

It was as a consequence of this situation, that a group of legal experts[2] coming from nearly all the Member States of the EU – and also from Switzerland – took the initiative themselves, and drafted a proposal for minimum harmonization in this area of law. There was no request from a Community institution that they should do this – although as is explained further below, the Commission had done work in this area in the past.[3] The Forum Europaeum, as the group has called itself, presented their proposal to the Commission in Brussels and the German Ministry of Justice.[4] An extract is published as a Document together with these Editorial Comments.[5]

The Commission had also worked on drafts for a harmonization of the law of corporate groups over an extensive period of time. This started in 1975, with the respective drafts regarding the statute of the Societas Europea[6] and ended in 1984 with the draft of a 9^{th} Directive on Corporate Groups.[7] The two proposals were rejected in the mid 1980s, for a number of reasons:

– partly because many Member States did not want a law governing corporate groups as such;
– more importantly, because the 1984 draft directive appeared to many Member States to be much too systematic, and thus insufficiently aware of the practical problems.

2. The experts who participated in the group were: Beusch (Munich), Le Cannu (Paris), Couturier (Paris), Denozza (Milan), Guyon (Paris), Helms (Heidelberg), Hohloch (Freiburg), Embid Irigo (Valencia), Jaeger (Milan), Kalss (Vienna), Kindler (Bochum), Konzen (Mainz), Lennarts (Groningen), Neye (Bonn), Nobel (Zurich), Ruiz Peris (Valencia), Prentice (Oxford), Rajak (Brighton), Rojo (Madrid), Scognamiglio (Rome), Skog (Stockholm), Theisen (Munich), Timmerman (Groningen), Treu (Milan), Vischer (Basel). The Organization Committee was made up of: Doralt (Vienna), Druey (St. Gallen), Hommelhoff (Heidelberg), Hopt (Hamburg), Lutter (Bonn), Wymeersch (Gent). The Steering Committee was made up of Hommmelhoff, Hopt and Lutter.

3. The group was supported by the Thyssen Foundation.

4. The German Ministry of Justice has organized an International Symposium on these proposals, to take place on 27 May 1999 in Bonn.

5. The complete text of the proposal consists of general legal political and legal comparative considerations, the concrete proposals to the Commission of the EC, and a statement of reasons. The text concluded with the "Theses" which are printed in the Document in this Review. The complete text has been published in German in 27 *Zeitschrift für Unternehmens- und Gesellschaftsrecht* (ZGR) (1998), 672–772. By now French and English translations have also been completed; they will be published in the *Revue de Sociétés* and in an independent publication, respectively, in the course of 1999; a translation into Italian and a publication in the *Rivista delle Societa* are also envisaged.

6. (Altered) proposal of a statute for the Societas Europea dated 30 April 1975, Enclosure 4/75 to the EC Bulletin, Arts. 223–240 d. (so-called organic constitution for corporate groups), also published in Lutter, *Europäisches Gesellschaftsrecht*, 1^{st} ed. (1979), pp. 278–357; see also Lutter (Ed.), *Die Europäische Aktiengesellschaft*, 2^{nd} ed. (Cologne 1978).

7. COM DOC No. III/1639/84, also published in 14 ZGR (1985), 446–465 and in Lutter, *Europäisches Unternehmensrecht*, 4^{th} ed. (1996), pp. 239–243 and 244–256.

Contrary to these much more far-reaching drafts of the Commission, the present proposal by the Forum is based on the principles of subsidiarity and minimum harmonization: no systematic law of corporate groups is proposed, instead individual parts have been extracted from national laws which could serve as elements of a European minimum harmonization:[8] only the solution of specific problems is proposed.

2. The proposals

We will now give a brief introduction to some of the specific problems the experts' proposal tries to deal with, and the elements which could provide a basis for this.

1. The parent company is continually making "proposals" to the subsidiary which, if put into effect, are advantageous to the group as a whole, but sometimes detrimental to the subsidiary. May the subsidiary's management follow these "proposals"? This difficult question – which has been answered differently by the laws of virtually all the Member States, was given a convincing solution by the French *Cour de Cassation* with what is known as the "Rozenblum formula".[9] This formula allows the parent company to make economically detrimental "proposals" to the subsidiary and to implement these "proposals", provided that three conditions are fulfilled:

- the corporate group must be closely guided;
- a coherent group policy must be followed;
- the advantages and disadvantages must be fairly distributed between the different companies.

This formula could provide a basis for selective harmonization in Europe, and could be helpful in solving the difficult relationship between the entrepreneurial majority of the parent company and the minority in the subsidiary. (See further theses 3 and 4, Document).

2. If the subsidiary still has minority shareholders, and the "Rozenblum formula" is accepted throughout the European Union, then this minority must also have legal means to control compliance with these rules. This is precisely the aim of the "special investigation", familiar to many national laws, but subject to very different regulations in the various States. Here, too, the proposal is for a minimum harmonization, so that minority shareholders do

8. The 1984 draft of a directive on corporate groups was a thorough and systematic proposal of almost 50 articles.

9. Cour de cassation (chambre criminelle) decision of 4 Feb. 1985, (1985) *Revue de Sociétés*, 648 et seq. (Bouloc); Cour de Cassation (chambre criminelle), decision of 13 Feb. 1989, (1989) *Revue de Sociétés*, 692 et seq. For more references see Forum Europaeum (*supra* note 4), esp. 27 ZGR, 705 et seq. and footnotes 164, 165.)

not simply have to trust that the Rozenblum formula is observed, but that they have the means to control its observance. (Theses 5 and 6, Document)

3. The law of corporate groups provides protection in two directions: to the creditors, and to the minority shareholders of the subsidiary. If the subsidiary does not have minority shareholders, then one problem is solved automatically. This is the basis for convincing regulations in the Belgian, French, Dutch and Austrian laws, according to which the smallest minorities – of 5% or less – may be excluded and compensated. This solution is taken over from the national laws. (Theses 9 and 10, Document)

4. The protection of minority shareholders is also the subject of many successful national regulations regarding takeovers. If a person or an enterprise acquires a relevant share of between 25% and 50%, the (in future) powerless minority will have the possibility to leave what is now a dependent company, and receive compensation. This rule – which is also part of the planned 13^{th} European Directive on Company Law[10] – is also adopted and proposed as a basis for renewed selective harmonization in the European Union. (Theses 7 and 8, Document)

5. The proposal suggests creating the possibility of legalizing a corporate group by means of a declaration of dependence. This would justify directions from the parent company, but would also lead to buy-out rights for minority shareholders, and to the contingent liability of the parent in a subsidiary's insolvency. If the Member States could be persuaded of the sufficiency of this model, corporate groups could be founded throughout the European Union – something which the (unsuccessful) Societas Europea has also striven for.

The proposal for a "group declaration" introduced in this respect has a variety of different aims and effects: it aims to give legal security to enterprises that lead corporate groups on a European scale, to secure a minimum standard of protection for creditors and minority shareholders, and to allow adequate disclosure. Thus, the requirements that the Common Market sets for effective enterprises are taken into account, and the investors in the European capital market – i.e. the shareholders – may rely on at least a minimum of protection of their interests in such corporate groups.

From an economic point of view, the declaration of the group leads to a kind of merger (insofar as it results in the right to give instructions, and the liability of the parent company for the subsidiary), but the participating companies remain legally unchanged. Therefore, this proposal does not entail problems in relation to co-determination: each company exists and continues to exist according to its national laws.[11]

10. Proposal for a 13th European Parliament and Council Directive on company law concerning takeover bids, O.J. 1996, C 295/01.

11. On the problem of co-determination, see Kolvenbach, *supra* note 1.

6. A final aspect deals with the important issue of the boundary of duties of group management and directors in the event of a financial crisis on the part of the subsidiary. Here, the concept of "wrongful trading" in English law[12] could be relevant, and could even be the basis of a rule connected with the "Rozenblum formula". In particular, in cases where the parent company has exercised its influence on the management of the subsidiary, the directors of the parent company are obliged to decide early on in the financial crisis of the subsidiary whether they want to reorganize it or liquidate it. If the directors delay this decision, they risk incurring the liability of the parent company for all debts of the subsidiary in case of its insolvency.

3. Concluding remarks

These comparatively few aspects – even when combined – do not result in a systematic law on groups. But their solution by means of an EC Directive would still suffice – when taken together with the regulations on group accounting and group disclosure which are already set out in the 7th EC Directive[13] – to harmonize and standardize the solutions to the most important legal problems in the relationship between the parent company and subsidiary. This would constitute an eminent service to the common market and to the security of the legal relations established in that market.

Marcus Lutter*

12. Sect. 214 III Insolvency Act with sect. 251 Insolvency Act ("Shadow director"): if the parent company exercises managerial control over the subsidiary and the subsidiary enters an economic and financial crisis without being promptly reorganized or liquidated by the parent company, the latter is liable for the debts of the subsidiary in the case of its insolvency.

13. 7th Directive on consolidated accounts (83/349/EC), O.J. 1983, L 193/1.

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