# 10 Years Cross-Border Mergers Directive: Some Observations About EU Border Protection and Minority Exit Rights

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## 1. INTRODUCTION

The 10th EU Directive on Cross-Border Mergers ('CBM Directive') has been in effect for ten years now. When it first entered into force, back in 2007, it inspired the Centre for European Company Law (CECL) to devote a conference to this matter in Utrecht, the Netherlands.[1] Recently my good friend professor Thomas Papadopoulos came with the brilliant idea to host a conference in Nicosia, Cyprus, to celebrate the second lustrum of the CBM Directive and to see where we currently stand. This contribution largely reflects my key note speech for that conference in which I address two aspects of the CBM Directive that, in my view, deserve some more attention of the European legislator.[2]

## 2. CALL FOR EU CORPORATE BORDER PROTECTION

I assume that, like many other countries, Cyprus has a keen interest in attracting investors from other EU jurisdictions by facilitating their efforts to become Cypriot companies: the inbound legal merger, as it is commonly known. Of course, it works the other way also: Cyprus companies can form outbound mergers with companies from other EU countries and so assume such other nationalities. Rumour has it that Cyprus immigration law makes it relatively easy for non-EU citizens to assume Cypriot nationality and enjoy EU recognition. Is this similar for non-EU companies?

A recent Study on the Law Applicable to Companies (hereafter 'Law Applicable to Companies Report'[3]) shows that Cyprus is one of the few EU Member States, besides Belgium, Malta, Portugal and Spain, that on the basis of specific legislation allows not only EEA-companies, but also non-EEA-companies to transfer their registered seat to its own jurisdiction. Such 'overseas company' could then be reregistered as a Cyprus company, or merge with a local Cyprus entity, and thus become a full-fledged Cyprus company. As a consequence, fulfilling just a few simple administrative requirements, for instance a Russian company could easily transform itself into a Cyprus company and then, by making use of the CBM-Directive, enjoy freedom of establishment within the EU.

As I said, this is allowed under the specific laws of just a few EU Member States, including Cyprus. However, in practice voluntary inbound reincorporations by way of transfer of seat of non-EU companies are also allowed in some other EU countries without any specific legislative basis, such as Luxemburg, Poland and Romania.[4]

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1 A report about this conference can be obtained from www.cecl.eu.

2 For an updated overview of European Company Law *see European Corporate Law* (Adriaan F. M. Dorresteijn ed., 3d ed., Kluwer Law International 2017), part 13 of the CECL book series. An elaborate survey of the implementation of the CBM Directive can be found in the Study on the Application of the Cross-Border Mergers Directive, performed by the Danish law firm Bech-Bruun, Lexidale, Sept. 2013 (hereafter: 'Bech-Bruun Report').

3 Final Report (June 2016): https://dx.doi.org/10.2838/527231. *See* about this report Carsten Gerner-Beuerle, Federico M. Mucciarelli, Edmund-Philip Schuster & Mathias M. Siems in their editorial in 14(4) ECL 148–149 (Aug. 2017)14(4).

4 Law Applicable to Companies report, Table 6, at 240–247. It is unclear whether Slovakia and Slovenia also allow the transfer of seat from non-EU countries, since the Report states that, although voluntary inbound reincorporations are allowed, these countries do 'follow the Cartesio and VALE rulings'.

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The point that I wish to make here is that once a non-EU company transforms itself into an EU company, either by undergoing a legal merger or by transferring its registered office, further progress into the European legal area becomes a simple matter of making use of the CBM Directive. The CBM Directive makes the creation of a 'safe' and well-guarded corporate border of the EU as a whole an unavoidable necessity. However, this in turn requires uniform and transparent national laws governing the inbound transfer of seat of non-EU companies and how local companies can merge with such companies. If any of these national laws are too permissive, or not composed with sufficient care, the result could be a kind of 'sluice', inviting non-EU corporate entities and interests to enter the EU without proper central control and oversight.

With large numbers of fugitives from war and poverty heading towards the EU, protecting the EU's border has become a topical issue. In my view, it is also an important topic in connection with the CBM Directive. However, the EU's corporate border does not follow the same line as its physical border, since corporate law is an integral part of any Member State's jurisdiction, wherever its location in the EU. A chain is only as strong as its weakest link. I am not suggesting in the least that Cyprus is this weakest link – it could just as well be another Member State, I simply do not know. Nor am I aware of any policy, initiative, or awareness of the European Commission in relation to this issue. What I do know is that a swift adoption of a Directive on the transfer of seat should be a matter of urgency, not only to harmonize the laws of the Member States within the EU, but also to protect the EU's corporate border from insufficiently controlled and undesired outside penetration.[5] The status of being an EU corporate entity is something that should be carefully preserved and not be acquired too easily. Therefore, in my view one cannot adequately focus on the migration of companies within the EU without paying sufficient attention to their immigration into the EU.

## 3. MINORITY EXIT RIGHTS

The CBM Directive sets out a wide array of rules and prescriptions to benefit minority shareholders in companies involved in cross-border mergers. In particular, those rules and prescriptions concern their right to be properly informed and consulted, their right to examine the documents drawn up by the company and the auditor involved, and last but not least their right to challenge majority decisions on both the merger itself and the valuation of their shares. Yet these are all general rules and principles that may be invoked by any shareholder. An exit right, conversely, is the only right connected specifically to the status of minority shareholder.

Does the CBM Directive grant minority shareholders a specific exit right? No, it does not. Neither does the Third EU Directive on local legal mergers.[6] Like Article 8(5) of the SE Regulation, Article 4 (2) of the CBM Directive merely states:

> *A Member State may, in the case of companies participating in a cross-border merger and governed by its law, adopt provisions designed to ensure appropriate protection for minority shareholders who have opposed the cross-border merger.*

As a consequence, some Member States have introduced an exit right in some form (withdrawal and cash compensation, or a buy-back obligation on the part of the disappearing company and/or the acquiring company), while others have not.[7]

So the CBM Directive does not prescribe an exit right for minority shareholders – and following an amendment adopted in 2009, in fact it now discourages Member States from introducing such right. A basic feature of the CBM Directive is that it demands compliance with the national merger laws on both sides of the transaction, i.e. for both the disappearing, merging company and the acquiring company, before the cross-border merger can be effected. However, following the 2009 amendment Article 10(3) contains a fundamental exception to that rule. It inter alia states that '*a procedure to compensate minority members*' in the law governing a merging company only applies if the other merging companies '*situated in Member States which do not provide for such procedure*' explicitly agree to that procedure when approving the draft terms of the merger.

Alarmingly, this means that, even if the merger terms do not make any provision for this issue, the minority shareholders in the disappearing company cannot invoke the exit and compensation rights granted to them by their own legislator.[8] This way the European legislator simply brushes aside any initiative that a Member State introduces in its own national law to provide adequate minority protection.[9] Member State laws that do not offer this protection are given preference over protective legislation.

5 *See* on the urge to harmonize within the EU e.g. Stephan Rammeloo, *A French-German Company Conversion (KG 21 March 2016): Another Call for Harmonizing the Laws on Cross-Border Company Migrations in Europe*, 14(4) ECL 177–184 (Aug. 2017).

6 The group of experts that has drafted the European Model Company Act supports this by commenting to s. 13.7 EMCA: 'Shareholders in general are sufficiently protected by the merger procedure, in particular by the expert's report confirming the share exchange ratio to be fair and reasonable. The group therefore considers that there is no need to suggest a mandatory sell-out right as a general rule in the model act. It should be left to the articles of association to provide for a sell-out right in such cases.'

7 As far as I have been able to establish, the following EU countries currently grant an exit right to minority shareholders in the event of an outbound cross-border merger: Austria, Cyprus, Czech Republic, Denmark, Estonia, Germany, The Netherlands, Poland, Slovak Republic, Greece. The following countries do not at present grant minority shareholders an exit right in a similar situation: Belgium, Bulgaria, France, Hungary, United Kingdom, Norway (EER). Cf. the country reports in the Bech-Bruun Report, *Cross-Border Mergers in Europe (Volume I)* (Dirk van Gerven General ed., Cambridge University Press 2010). *See also* Marieke Wyckaert & Koen Geens, *Cross-Border Mergers and Minority Protection: An Open-Ended Harmonization*, 5(6) ECL 288–296 (Dec. 2008). For France, *see* Raluca Papadima, *Appraisal Activism in M&A Deals: Recent Developments in the United States and the EU*, 12(4) ECL 188–198 (Aug. 2015).

8 Cf. Dirk van Gerven, o.c., par. 30.

9 Except, I presume, where the national law transposes Art. 28 of the 3rd EU Directive, which grants minority shareholders an exit right in the event of a simplified 90% parent–subsidiary merger, or where the Member State specifically opts for minority protection in cross-border mergers in the wake of Art. 4(2) of the CBM Directive.

I fear that in practice Article 10(3) might have the effect of "an invitation" to majority shareholders and their representatives on the board in a protective jurisdiction to form a cross-border merger with an SPV, incorporated by such majority shareholder(s), in a non-protective jurisdiction. This would force the minority shareholders to choose between remaining in an unfamiliar legal environment and selling their shares for less than fair value.

It should be noted that a cross-border merger brings with it a fundamental change in legal environment for the shareholders: not only as regards corporate governance, but also in terms of settling legal disputes and corporate litigation, relationships with workers' unions and other employee representatives when applicable, the rules for challenging corporate resolutions, the role of notaries and other officials in corporate relations, etc.[10] Obviously, this effect of 'alienation' from the company's legal environment will be stronger for shareholders of a closed, locally oriented company than for often foreign investors in a publicly listed company.[11] Nevertheless, in my opinion, the minority shareholders' exit right in a cross-border merger is a fundamental right that should be recognized in the CBM Directive, if not in the Shareholder Rights' Directive itself.

10 In this context, I find it quite understandable that the Netherlands has indeed introduced a mandatory exit right for dissenting minority shareholders in the event of a cross-border legal merger (Art. 2:333h DCC), but no such right in case of a local merger.

11 Cf. Marieke Wyckaert & Koen Geens, *supra* n. 7, at 295.