CORPORATE MIGRATION IN THE EUROPEAN UNION

AN ANALYSIS OF THE PROPOSED 14TH EC COMPANY LAW DIRECTIVE ON THE TRANSFER OF THE REGISTERED OFFICE OF A COMPANY FROM ONE MEMBER STATE TO ANOTHER WITH A CHANGE OF APPLICABLE LAW

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I. INTRODUCTION[1]

For many years, efforts have been made to establish a single market without internal frontiers or barriers in the European Union (EU). In spite of this, it has not been possible to this day to secure corporations the freedom to migrate across the borders of the EU Member States. This is in stark contrast to the situation in the United States (US).

In the US, it is generally possible to choose between the corporate laws of the different states when intending to incorporate a corporation. When the decision has been made to incorporate a corporation in one state, there is nothing to prevent the corporation from subsequently conducting its activities in a state other than the state of incorporation. Consequently, there is rarely a motive for incorporating the corporation in another state,[2] but if this is desired, such reincorporation may be effected with little cost or difficulty.[3]

However, the conflict of laws rules applied to corporations in several EU Member States prevent the free choice of deciding where to incorporate, because the rules usually require that the corporation has to be incorporated in the state in which

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[1] The authors would like to thank Professor James D. Cox, Duke Law School, for commenting on an earlier draft of this article. Abbreviations for the most widely consulted European law journals: AG: Die Aktiengesellschaft; BB: Der Betriebsberater; DB: Der Betrieb; EuZW: Europäische Zeitschrift für Wirtschaftsrecht; IPRax: Praxis des internationalen Privat- und Verfahrensrecht; JuS: Juristische Schulung; JZ: Juristenzeitung; NJW: Neue Juristische Wochenschrift; NZG: Neue Zeitschrift für Gesellschaftsrecht; RabelsZ: Rabels Zeitschrift für ausländisches und internationales Privatrecht; RIW: Recht der Internationalen Wirtschaft; ZGR: Zeitschrift für Unternehmens- und Gesellschaftsrecht; ZHR: Zeitschrift für das gesamte Handels- und Wirtschaftsrecht; ZIP: Zeitschrift für internationales Privatrecht; ZvglRWiss: Zeitschrift für vergleichende Rechtswissenschaft.

[2] However, changes in the corporate law to which the corporation has so far been subject may motivate reincorporation. Cf. James D. Cox, Thomas Lee Hazen & Hodge O'Neal, 1 Corporations §3.2 (2000); The reason could also be that the corporation wants to implement activities (merger, acquisition, anti-takeover defense, etc.) that would be easier or less expensive to implement under the corporate law of another state. See Roberta Romano, The Genius of American Corporate Law 32 (1993); and Clark D. Stith, Federalism and Company Law: a "Race to the Bottom" in the European Community, 79 Geo. L.J. 1581, 1606 (1991).

[3] See Romano, supra note 2, at 34; Stith, supra note 2, at 1599; and Brian R. Cheffins, Company Law: Theory, Structure and Operation 423 (1997).

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it has its real seat.[4] The same conflict of laws rules also prevent a corporation from subsequently moving its activities (and thus its real seat) to another Member State.

A corporation may of course reincorporate by transferring its activities to a newly formed corporation in another Member State, but such a transaction will be very costly and difficult in the EU. Even though the corporate rules governing both private and public limited companies have been extensively harmonized, this harmonization still has not provided a real possibility for corporate cross-border migration.[5] In certain areas, the rules have been harmonized to establish minimum standards that ensure relatively uniform rules in the EU Member States.[6] This approximation of laws does not in itself ensure that corporations can make cross-border movements, and therefore a number of proposals have been directed at this particular aspect of corporate law–for example the proposal for a Directive on cross-border merger, a Regulation on a European Company, etc.[7]

The proposal for a Fourteenth European Community (EC) Company Law Directive on the transfer of the registered office of a company from one Member State to another with a change of applicable law is another attempt to ensure the right of free movement of corporations.[8] The proposed Directive will make it possible for corporations in the EU to effect an identity-preserving nationality change, whereby a corporation that is incorporated in one Member State (the state of departure) may be incorporated in another Member State (the state of arrival) without having to be dissolved in the state of departure and then reincorporated in the state of arrival. The aim thus is to ensure the possibility of cross-border migration. Such a migration is not equivalent to "reincorporation" in the sense in

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[4] Further on this subject, see infra section II.B.

[5] Most EU Member States have a corporate form for large, publicly-held, and often listed, corporations and another corporate form for small, privately-held corporations. The former is represented by, *inter alia*, the UK public limited company, the German *Aktiengesellschaft*, and the French *Société Anonyme*. The latter corporate form is represented by, *inter alia*, the UK private limited company, the German *Gesellschaft mit beschränkter Haftung* (GmbH), and the French *Société à responsabilité limitée* (SARL). In this text, the term "corporation" is used to refer to the former, publicly-held type unless otherwise stated.

[6] Approximation of laws has been effected, *inter alia*, concerning the rules of corporate registration (First EC Company Law Directive, 68/151, 1968 O.J. (L 65) 8); the capital requirements in public limited companies (Second EC Company Law Directive 77/91, 1977 O.J. (L 26) 1); the rules on (internal) mergers, i.e. mergers between corporations from the same Member State (Third EC Company Law Directive, 78/855, 1978 O.J. (L 295) 36); and harmonization of the rules on annual accounts and consolidated accounts by the Fourth and the Seventh EC Company Law Directives (78/660, 1978 O.J. (L 222) 1, and 83/349, 1983 O.J. (L 193) 1, respectively). For a further account of the harmonization of the corporate law in the EU, see e.g. Erik Werlauff, EC Company Law (1993); and Vanessa Edwards, EC Company Law (1999).

[7] See also comments infra section IV.

[8] So far, there are two proposals for the Directive. The first is dated April 22, 1997 (internal doc. XV/6002/97) and published in ZIP (1997), p. 1721 et seq.; the latest proposal, which is the one referred to in the following text, is dated November 11, 1997 (internal doc. XV/D2/6002/97-EN REV1) [hereinafter Proposed Fourteenth EC Company Law Directive]. Neither proposal has been adopted by the European Commission, and they are therefore not official proposals and have not been published in the Official Journal.

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which this concept is used in the USA, and below the phenomenon is referred to as corporate change of nationality.[9]

To make it possible to assess the impact of the proposed Directive, it is necessary briefly to explain the current rules in the EU. Section II contains a short description of the problems in connection with the existing corporate conflict of laws rules, and section III is concerned with the existing rules of the Member States governing a corporate change of nationality. Sections IV-VII contain a discussion of the background to and the content of the proposed Directive.

II. CONFLICT OF LAWS RULES RESTRICTING THE FREEDOM OF ESTABLISHMENT

As mentioned above, the Member States do not agree on the criteria that are to form the basis for determining which corporate law is to govern a corporation.

A. Incorporation Theory

Some Member States–for instance the Netherlands, Ireland, Denmark and United Kingdom (UK)–apply the incorporation theory. According to this theory, as a general rule,[10] a corporation is subject to the regulation of the country in which it is incorporated.[11] It is immaterial whether, after incorporation, the corporation does business or has its head office in the country of incorporation. The decisive factor is whether it has been formed in accordance with all the legal requirements of the country of incorporation.

The application of the incorporation theory makes it easy to determine the jurisdiction to which the corporation is subject. Under this theory a corporation is free to locate its head office (management seat) where it is most advantageous, something which is important if it is desired to develop the single European market. The incorporation theory involves the "risk" that it may in turn lead to competition among the Member States in terms of introducing the most permissive corporate law rules with a view to attracting as many corporations as possible–which in the European debate is referred to as the Delaware syndrome.[12]

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[9] The concept of "reincorporation" appears to be used by American scholars as a general term for a transaction, which eventually results in the continuance of corporate activities in a corporation subject to the laws of another state. One of the most widely used methods of reincorporation appears to be when a corporation incorporates a subsidiary in another state and subsequently merges into it. See Romano, supra note 2, at 34.

[10] Exceptions may be made where a corporation is formed in one country with a view to circumventing the corporate law of another country. As to circumvention, see Paul Krüger Andersen and Karsten Engsig Sørensen, Free Movement of Companies from a Nordic Perspective, 6 The Maastricht Journal of European and Comparative Law 47, 57-58 (1999); and Mette Neville, Aktieselskabers tilknytning, Juristen 145, 151 (1997), with references.

[11] All EU Member States normally require a corporation to be registered in order for it to be validly formed. Therefore, a corporation is regarded as being incorporated in the Member State in which it is registered.

[12] See section II.C below.

B. The "Siège Réel" Theory

Other Member States, for instance Germany, France and Portugal, apply the *siège réel* theory when determining the jurisdiction to which a corporation is subject in terms of corporate law.

According to the *siège réel* theory, a corporation is subject to the laws of the country in which it has its *de facto* head office; the corporation is further required to register in that country in order to acquire legal personality.

1. Determination of the *Siège Réel*

The determination of the concept of "head office" is the sore point of the *siège réel* theory, as the concept is far from unambiguous.[13] The application of the theories is further complicated, because the EU Member States applying the *siège réel* theory interpret the concept differently. Today most Member States applying the *siège réel* theory appear to define the head office as the management seat. However, the management seat is also an ambiguous concept and gives rise to two problems: (1) who is the management of the corporation, and (2) what does "have its seat" mean? The management of the corporation may mean, *inter alia*, (a) the person who has the *de facto* control and influence, e.g. a controlling majority shareholder including a parent corporation, or (b) the body in charge of the actual day-to-day management of the corporation, e.g. the management board/board of directors of a corporation. The major opinion in international theory appears to regard the management board/board of directors as the management of the corporation.

The question is then: Where is the management seat located? It may be where decisions concerning internal affairs are made, i.e. where the management meets and decides, or where the decisions are "carried out." If the management seat is defined as the place where the management makes internal operational decisions, substantial problems arise as the place may vary from one decision to another. Moreover, some corporations have "divided" management, i.e. the management is located in more than one state.[14] This may be the case where the members of the management are resident in different states and communicate by telephone, fax, e-mail etc., or because board meetings are alternately held in different states. If the management seat is defined as the place where decisions are made, the seat then cannot be located for certain; so the question is whether it is possible to lay down a gap-filling rule according to which the management seat is located in the state of incorporation.

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[13] The problems of defining the concept are exacerbated by the increasing internationalization. See e.g. Günther Grassmann, System des internationalen Gesellschaftsrechts 114 (1970); Otto Sandrock, Multinationale Korporationen im internationalen Privatrecht 180 (1978); Sandrock, Die Konkretisierung der Ûberlagerungstheorie in einigen zentralen Einzelfragen, *in* Festschrift für Günther Beizke 669, 671 (1979); Matthias Schümann, Die Vereinbarkeit der Sitztheorie mit dem europäischen Recht, 9 EuZW 270 (1994); Viola Kruse, Sitzverlegung von Kapitalgesellschaften innerhalb der EG 23 (1997); Stephan Travers, Der Beweis des Anknüpfungskriterium "tatsächlicher Sitz der Hauptvervaltung" im Internationalen Gesellschaftsrecht (1997); Thomas Panthen, Der "Sitz"-Begriff im internationalen Gesellschaftsrecht (1988); and Rüediger, Der Nachweis des Verwaltungssitzes ausländischer juristischer Personen (1997).

[14] See e.g. Grassmann, supra note 13, at 368 et. seq.; and Sandrock, supra note 13, at 685 et. seq.

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Problems may be almost insurmountable for international groups of corporations as they are often centrally organized, so that the overall operational guidelines are set forth by the parent corporation and given to and carried out by the subsidiary. If priority is given to the place of decision-making, the head office of the subsidiary will be located in the state in which the parent corporation is located.[15] Regardless of whether one or the other definition is applied, it will be almost impossible for the management of the corporation and any contracting party to determine where the corporation has its seat, something which is very unfortunate considering the serious consequences the *siège réel* theory may have.

2. Consequences of the *Siège Réel*

If a corporation that is registered in a Member State applying the *siège réel* theory, for instance Germany, wants to move its head office to another Member State, German law provides that the corporation is subject to the laws of the state of arrival. According to the most widely held opinion in German legal theory, the result is that the corporation no longer can be recognized as a separate legal person in Germany, so it has to be dissolved, either voluntarily or compulsorily.[16] A transfer of the head office requires dissolution of the corporation in the state of departure (Germany) and reincorporation in the state of arrival.

If a corporation, for example a UK private limited company which is incorporated in the United Kingdom, wants to move its head office to Germany, Germany, as the state of arrival, will assume that it is a German corporation subject to German law, as its head office is situated in Germany. But as it is not incorporated in Germany, the corporation will have no legal personality, and as a consequence, the shareholders cannot claim limited liability.[17] If the state of departure or the state

[15] Several of these problems may be solved by focusing, as in Germany, on the place where the management bodies "convert" the fundamental operational decisions to "Geschäftsführungsakte" (acts of business management); see Bundesgerichtshof (BGH), DB 219 (1986); Oberlandesgericht (OLG) Hamburg, RIW 816 (1988); OLG Bayern (1986), p. 1325 et seq.; Landgericht (LG) Marburg Sept. 17, 1992, 1 O. 115/92 reported in 10 AG 472 (1993). As for groups, the management seat will basically be placed where the central administration of the subsidiary is located. See Herbert Wiedermann, Band, I Gesellschaftsrecht 800 (1980); and Christian von Bar, Internationales Privatrecht 451 (1991).

[16] See e.g. Kruse, supra note 13, at 37. However, German authors have questioned whether there is a legal basis for dissolving a corporation moving its head office. Brigitte Knobbe-Keuk argues that a corporation that has acquired legal personality through registration cannot be deprived of this as long as the corporation has its registered office in Germany. Knobbe-Keuk, Umzug von Gesellschaften in Europa, 154 ZHR 325, 351 (1990). Similarly, Belgium and Spain appear to assume that a corporation must be dissolved if it moves its head office out of the country. Carsten Thomas Ebenroth and Uwe Eyles, Die innereuropäische Verlegung des Gesellschaftssitzes als Ausfluss der Niederlassungsfreiheit, 7 DB 363, 368 (1989); and Moris Lehner, Die Stuerliche Ansässigkeit von Kapitalgesellschaften, 3 RIW 201 (1988); for a critical discussion, however, see Hans-Georg Berg, Die GmbH im Strudel der Sitztheorie, 24 GmbHR 1136 (1997).

[17] However, agreements on the mutual recognition of corporations have been made, as, *inter alia*, between the United States and Germany. See Treaty of Friendship, Commerce and Navigation, with protocol and exchanges of notes. Signed at Washington October 29, 1954, entered into force July 14, 1956. 7 UST 1839; TIAS 3593; 273 UNTS 3. Further on this treaty, see Carsten Thomas Ebenroth and Birgit Bippus, Die Anerkennungsproblematik im Internationalen Gesellschaftsrecht – Am Beispiel des Freundschafts-, Handels-, und Schiffartvertrages zwischen der Bundesrepublik Deutschland und den Vereinigenten Staten von Amerika vom 29.10.1954, 35 NJW 2137 (1988); Norbert Walter, 2

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of arrival–or both–applies the *siège réel* theory, and therefore does not allow a corporation to be incorporated in one state while its head office is located in another state, a corporation wishing to relocate its head office will typically be forced to change its nationality if it wants to remain a corporation.[18]

It follows from the foregoing discussion that the migration of a corporation is hindered by the *siège réel* theory, and that the theory also unduly restricts the freedom of establishment under the Treaty of Rome (EC Treaty, or TEC).[19]

C. General Considerations behind the Siège Réel Theory

The *siège réel* theory is often characterized as a *protection theory*.[20] It aims to ensure that a corporation whose head office is in a particular country is governed by its mandatory corporate law rules protecting interest groups such as shareholders (typically minority shareholders), creditors and employees.[21] The key argument for the *siège réel* theory is the desire to avoid the so-called Delaware syndrome. In several Member States it is widely believed that the use of the incorporation theory will lead to a statutory "race to the bottom" involving a reduction in the protection of important interest groups, e.g. minority shareholders and creditors in the state of the head office.[22]

Abhandlungen zum Steuer- und Abgabenrecht (1992); and Bar, supra note 15, at 456. Under the treaty, Germany recognizes a US corporation when it moves its head office from one US state to another, as well as when the corporation moves its head office to Germany. The treaty makes the *siège réel* theory inoperative. See, e.g., Carsten Thomas Ebenroth, Gaining Access to Fortress Europe – Recognition of U.S. Corporation in Germany and the Revision of the Seat Rule, 24 The International Lawyer 459, 469 (1990). Under the treaty the law of the state of incorporation applies. See Carsten Thomas Ebenroth and Thomas Auer, Grenzüberschritende Verlagerung von unternehmerischen Leitungsfunktionen im Zivil- und Stuerrecht, 3 RIW, Beilage 1, 241 (1992).

[18] The loss of legal personality as a private limited company does not mean that the corporation is non-existent according to German law. The corporation may qualify as another German corporate form, for instance a partnership (*offene Handelsgesellschaft* oHG). Cf. Horst Eidenmüller and Gebhard Rehm, Gesellschafts- und Zivilrechtliche Folgeprobleme der Sitztheorie, 1 ZGR 89, 90 (1997), who also discuss some of the consequences, e.g. as to liability, of a foreign corporation moving its head office to Germany without being registered there. Further on this subject, see Jürgen Köster, Rechtsträgerschaft und Haftung bei Kapitalgesellschaften ohne Verwaltungssitz im Gründungsstat, 7 NZG 241 (1998).

[19] See further infra section II.D.

[20] See, e.g., Peter Behrens, Niederlassungsfreiheit und Internationales Gesellschaftsrecht, 52 RabelsZ 498, 512 (1988); Schümann, supra note 13, at 269; and Wulf-Henning Roth, Recognition of Foreign Companies in Siege Réel Countries: A German Perspective, *in* Current Issues on Cross-Border Establishment of Companies in the European Union 29, 31 (Jan Wouters & Hildegard Schneider eds., 1995).

[21] See, e.g., Karsten Engsig Sørensen, Samarbejde mellem selskaber i EF 73 (1993); and Neville, supra note 10, at 147. In addition, the public interest in controlling business is intended to be considered, and the state which is mostly affected by the corporation of course has the greatest interest. See, e.g., Schümann, supra note 13.

[22] American authors do not agree, however, whether such competition will necessarily lead to a loss of quality in terms of legislation. Several authors, including European scholars, believe that the competition will put pressure on legislators and ensure a continuing adaptation of corporate laws as the needs of business change, thereby ensuring the development of the best laws. On this debate see Sandrock, supra note 13, at 227; Hanno Merkt, Das Europäische Gesellschaftsrecht und die Idee des "Wettbewerbs der Gesetzgeber," 59 RabelsZ 545 (1995); Jonathan I. Charney, A Reader on the Law of Business Enterprise 365-402 (1994); Roberta Romano, Explaining American Exceptionalism in Corporate Law, in International Regulatory Competition and Coordination 127 (William W. Bratton,

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German scholars often cite the rules on employee participation as the main argument for the *siège réel* theory. German law provides that the employees of a corporation with more than 500 employees are entitled to be represented on the supervisory board, whereas other countries, such as the United Kingdom, do not have rules on employee participation.[23] The Germans fear that their system will be diluted if it is possible for German corporations to migrate to countries with less burdensome rules. In German theory such migration is called "*Flucht aus der Mitbestimmung*," i.e. flight from codetermination.[24] The *siège réel* theory currently affords protection against such migrations, as a German enterprise cannot use a foreign corporate form if the real seat is located in Germany, because in such cases Germany will treat the corporation as being subject to German law.

The *siège réel* theory is thus partly motivated by the fear of circumvention or avoidance of mandatory corporate law rules. It may be questioned whether the considerations behind the *siège réel* theory should be given priority over the interest in creating a single European market. In particular, it is doubtful whether the *siège réel* theory can be maintained in light of the increasingly advanced harmonization of corporate law in the European Union. One result of this harmonization is substantial conformity between the laws of the Member States that regulate the type of corporation called public limited company and, by definition, these common minimum rules cannot be circumvented.[25]

Some European scholars have further argued that it is possible to find a solution which takes account of minority and creditor protection as well as the German rules on employee participation, and which have less impact on the free movement of corporations than the *siège réel* theory. For instance, it is possible to imagine a solution corresponding to that applied in some US States, and which provides that part of the corporate laws of these States apply to corporations incorporated in other states if they can be deemed to be "pseudo-foreign corporations."[26] A similar solution is applied in the Netherlands where the legislature recently passed a Pro

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Joseph McCahery, Sol Picciotto and Colin Scott eds., 1998); Harm-Jan de Kluiver, European and American Company Law. A Comparison after 25 Years of EC Harmonization, 1 Maastricht Journal of European and Comparative Law 139 (1994); Stith, supra note 2; and Ronald J. Gilson, Corporate Governance and Economic Efficiency, *in* Aspects of Corporate Governance 131 (Mats Isaksson and Rolf Skog eds., 1994).

[23] The provisions on employee participation are found in several acts, e.g. the Betriebsverfassungsgesetz (BetrVG) and the Mitbestimmungsgesetz (MitbestG). Corporations with more than 2000 employees generally are governed by the MitbestG, according to which half the members of the supervisory board must be employee representatives. There is no requirement for employee participation for corporations formed after August 10, 1994 and which have fewer than 500 employees.

[24] See also comments in section VI infra.

[25] See e.g. Axel Steiger, Grenzüberschreitende Fusion und Sitzverlegung von Kapitalgesellschaften innerhalb der EU nach spanischem und portugiesischem Recht 50 (1996); Kruse, supra note 13; and Neville, supra note 10, at 161.

[26] See on this subject Erwin R. Latty, Pseudo-Foreign Corporations, 65 Yale L. J. 137 (1955); and William J. Carney, The Political Economy of Competition for Corporate Charters, *in* Wouters & Schneider, supra note 20, at 249. For instance, Section 2115 of the California Corporations Code provides that a number of its provisions apply to foreign corporations if the average of the property factor, the payroll factor, and the sales factor in California is more than 50 percent during the latest full income year. This is also the case where more than one-half of its outstanding voting shares are held by persons resident in California.

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Forma Foreign Companies Act, which came into force in January 1998.[27] The Act was motivated by the many examples in which corporations incorporated in another country exclusively or mainly did business in the Netherlands. One reason for this activity was the very high Dutch minimum capital requirement. In contrast, the UK private limited companies have proven particularly popular, as there is no corresponding minimum capital requirement in the UK. A pro forma corporation is one that is incorporated in a country other than the Netherlands, and "which conducts its business entirely or almost entirely in the Netherlands without any further real tie with the state under whose law it was incorporated." Such pro forma corporations are required to be registered in the Netherlands and therefore must comply with a number of corporate law rules, including in particular the minimum capital requirement.[28] Non-compliance with these requirements will make the directors of a corporation liable jointly and severally together with the corporation for any legal act performed by the corporation in the period of non-compliance with the Dutch requirements.

In Denmark, the Trade and Companies Board[29] has refused to register a number of branches of foreign corporations.[30] These cases involved English private limited companies (Ltd.) owned by Danish business operators who wanted to register a branch with a view to doing business in Denmark without pursuing any activity in the United Kingdom.[31] However, in the *Centros* case, the European Court of Justice found this practice to be contrary to Articles 43 and 48 (former Articles 52 and 58) of the EC Treaty governing the freedom of establishment.[32] In its judgment, the European Court of Justice holds that a situation in which a corporation wants to establish a branch in another Member State is covered by the provisions on the freedom of establishment in the EC Treaty even if the corporation carries on its entire business in a state other than the state of incorporation. The judgment emphasizes that it is immaterial that the branch was established for the purpose of avoiding minimum capital requirements in Danish company law.

[27] Act of Dec. 17, 1997, "Wet op de formeel buittenlandse vennotschappen," Stbl. 699; further on the Act see Levinus Timmerman, Sitzverlegung von Kapitalgesellschaften nach niederländischem Recht und die 14. EU-Richtlinie, Sonderheft ZGR 147 (1999). The Bill for the same Act is discussed by Stephan Rammeloo, Recognition of Foreign Companies, *in* Wouters & Schneider, supra note 20, 47, at 57.

[28] Id. at section 4.

[29] The administrative body responsible for the incorporation of companies.

[30] The Eleventh EC Company Law Directive (89/666 EEC) (1989 O.J. (L 395) 36) specifies the disclosure requirements in respect of branches of public and private limited companies. The Directive does not only apply to companies from other Member States but also to companies from non-Member States. Most Member States have restricted their regulation of branches of foreign companies to requirements of registration and disclosure.

[31] The reason for incorporating an English private limited company is that the United Kingdom does not require the provision of a minimum share capital in a Ltd., whereas a minimum capital of DKK125,000 (approximately US$15,000) is required under Danish law.

[32] Centros Ltd. v. Erhvervs- og Selskabsstyrelsen, Case C-212/97, [1999] E.C.R. I-1459, [1999] 2 C.M.L.R. 551.

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D. The Siège Réel Theory in an EU Perspective

As mentioned earlier, the *siège réel* theory is a general obstacle to the free movement of corporations and thus the creation of the single European market. The question then arises whether the *siège réel* theory is incompatible with Articles 43 and 48 of the EC Treaty on the freedom of establishment. According to Article 43, a person from an EU Member State is free to do business in another Member State on terms identical with those enjoyed by the nationals of the state of arrival. The freedom of establishment provided by Article 43 exclusively applies to natural persons, but is extended by Article 48 so that it applies correspondingly to corporations formed in accordance with the laws of a Member State.[33]

The question whether Article 48 of the EC Treaty protects the freedom of establishment of a corporation in the event of a transfer of the head office to another Member State was tried by the European Court of Justice in the *Daily Mail* case.[34] It was held that Article 48 of the EC Treaty does not provide protection of this kind of establishment, and the Court specifically accepted the application of the *siège réel* theory which has as its consequence the dissolution of a corporation that moves its head office. The European Court of Justice argued that this part of the freedom of establishment requires harmonization of corporate law rules, either by way of an international agreement, as mentioned in Article 293 (former Article 220) of the EC Treaty, or by way of a directive in pursuance of Article 44(2)(g) (former Article 54(3)(g)) of the EC Treaty.[35]

All attempts to "put down" the *siège réel* theory through arguments based on the Treaty of Rome therefore appear to have failed.[36] As a result of these unsuccessful

[33] To be governed by the freedom of establishment, the corporation must be formed in accordance with the law of a Member State, and there must be a further link to the EU. Cf. TEC art. 48. Either the corporation's registered office, central administration or the principal place of business must be within the Community. It is further required that the activity of a corporation must show a real and continuous link with the economy of a Member State. For a more detailed discussion of the freedom of establishment, see e.g. Karsten Engsig Sørensen and Poul Runge Nielsen, 1 EU-retten 401-460 (1999), Paul R. Craig and Grainne de Búrca, EU Law, Text Cases and Materials 727-761 (2d ed., 1999), and Stephen Weatherill and P.R. Beaumont, EU Law 671-714 (3d ed., 1999).

[34] Regina v. H.M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail & General Trust Plc, Case 81/87, [1988] 3 C.M.L.R. 713, [1988] E.C.R. 5483. See further Andreas Reindl, Companies in the european community: Are the Conflict-of-Law-Rules ready for 1992, 11 Mich. J. Int'l L. 1270 (1990); Engsig Sørensen, supra note 21, at 91; Ludwig von Bar, supra note 15, at 458; Helmut Grothe, Die ausländische Kapitalgesellschaft & Co. 125 (1989); Ebenroth & Eyles, supra note 16, at, 413; Otto Sandrock and Andreas Austmann, Das Internationale Gesellschaftsrecht nach der Daily Mail-Entscheidung des Europäischen Gerichtshof: Quo Vadis?, 4 RIW 249 (1989); Runge Nielsen, Services and Establishment in European Community Banking Law 148 (1994).

[35] TEC art. 293 reads as follows: "Member States shall, so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals [...] the mutual recognition of companies or firms [...] the retention of legal personality in the event of transfer of their seat from one country to another."

[36] It may be argued that time and development have reduced the importance of the judgment. As argued by Schümann, supra note 13, at 271, the European Court of Justice explicitly based its decision on the state of Community law as it was then. Since 1988 the harmonization process in the field of corporate law and the general development of the European Community have made great strides, particularly concerning the creation of the single market. The current importance of the *Daily Mail* decision should be seen in that light.

attempts to solve the problem at a supranational level, a number of EU Member States have, as an alternative, established various models for an identity-preserving change of nationality as part of their national laws.[37]

The judgment of the European Court of Justice in *Centros*, mentioned in section II.C above, probably does not change the rule laid down in the *Daily Mail* decision either. The judgment in *Daily Mail* concerned the consequences of the rules of private international law, whereas *Centros* concerned the question whether Member States may prevent circumvention of company law rules by making foreign corporations subject to certain requirements. Nothing in the grounds for the decision implies that the European Court of Justice intended to overrule the judgment in *Daily Mail*; the judgment in *Daily Mail* is not even mentioned, neither in the Opinion of the Advocate General nor in the judgment itself. If the European Court of Justice had intended to overrule one of its most controversial judgments, it would have considered it in the grounds for its decision. Accordingly, Member States that apply the *siège réel* theory probably will be able to continue applying it after the judgment in *Centros*.[38]

However, the result of the judgment of the European Court of Justice may be that Member States can only impose requirements on pseudo-foreign corporations if this is justified by imperative requirements in the general interest, and if the other conditions for imposing restrictions under EU law have been met.[39] This may mean that the Dutch act mentioned above in section II.C is contrary to Articles 43 and 48 of the EC Treaty.

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[37] Cf. infra section III.A.

[38] See also Peter Kindler, Niederlassungsfreiheit für Scheinauslandsgesellschaften, 28 NJW 1993 (1999); Werner F. Ebke, Die Schicksal der Sitztheorie nach dem Centros-Urteil des EuGH, 13 JZ 656 (1999); and Karsten Engsig Sørensen, Prospects for European Company Law after the Judgment of the European Court of Justice in Centros Ltd., *in* Cambridge Yearbook of European Legal Studies, vol. 2 (Alan Dashwood and Angela Ward eds., 2000); but for a contrary view see Erik Werlauff, Udenlandsk selskab til indenlandsk aktivitet, 16 Ugeskrift for Retsvæsen 163 (1999); Robert Freitag, Der wettbewerb der Rechtsordnungen im Internationalen Gesellschaftsrecht, 9 EuZW 267 (1999); and Jörg Risse, Zwingende Eintragung der Zweigniederlassungen von Gesellschaften, 12 Monatsschrift für Deutsches Recht 752 (1999).

[39] The European Court of Justice has specified the following four conditions: (1) Domestic and foreign companies must be treated equally; (2) the measures must be justified by imperative requirements in the general interest; (3) the measures must be suitable for securing the attainment of the objective that they pursue; and (4) they must not go beyond what is necessary in order to attain it. In *Centros*, the European Court of Justice stated, *inter alia*, that conditions 3 and 4 had not been fulfilled. The requirement that the corporation had to do business in the United Kingdom did not constitute effective protection of the Danish rules on a minimum share capital. If the corporation had done business in the United Kingdom, the Danish Commerce and Companies Agency would be obliged to register the branch, even though the Danish minimum capital requirements had not been met. By contrast, the Agency would have to refuse to register a branch even though the corporation had been incorporated in the United Kingdom with a capital of, for instance, £100m if the corporation did not do business in the United Kingdom. In connection with condition 4, the European Court of Justice found that the Danish Government could have safeguarded the same interests by adopting less restrictive measures. See *Centros*, supra note 32, at para. 38. The Court refers to measures making it possible for public creditors to obtain the necessary guarantees.

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III. EXISTING POSSIBILITIES OF CHANGE OF NATIONALITY

As the *siège réel* theory often prevents a corporation from transferring its activities and thus its head office, the only alternative is for the corporation to change its nationality.[40] However, a nationality change is only a real alternative if the corporation can be registered in another country and acquire a new nationality without having to be dissolved in the state of departure and reincorporated in the state of arrival (identity-preserving nationality change). A change of nationality requiring dissolution in the state of departure, whereby assets are transferred to the shareholders, and reincorporation in the state of arrival, involving a transfer of assets to the newly formed corporation, is costly and a non-feasible method, both in terms of corporate law and tax law.[41] The tax implication will be that the corporation is taxed as if it were liquidated.[42] The corporate law rules will treat it as a different corporation, and therefore, contracts, loans, etc. cannot be assigned to the new corporation without the consent of the creditors, lenders or contracting parties.

Currently, a corporation can only make an identity-preserving nationality change if there is a legal basis for doing so in the national laws of the Member States concerned or in international agreements.[43] This means that the law of the state of departure allows the corporation to change its nationality without dissolution. If the state of departure allows the corporation to retain its legal personality, it depends on the law of the state of arrival whether the change of nationality can be effected without reincorporation.[44]

There are substantial differences in how the Member States as states of departure deal with an identity-preserving nationality change. German case law and a majority of German authors[45] take the view that the corporation has to be dissolved when changing its nationality, and therefore, an identity-preserving nationality change is *prima facie* impossible.[46]

Similarly, each Member State takes its own special position as to whether, as the state of arrival, it requires reincorporation if a corporation is desirous of moving to that state. German law requires reincorporation, and consequently, a foreign

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[40] As all EU Member States require that corporations of the types public and private limited companies have their registered office in the state of incorporation, a change of nationality involves the relocation of the registered office. A solution which allows a corporation to be registered in two or more states at the same time may be possible, but such multiple incorporation apparently is not recognized by the EU Member States. Further on this subject see P. St.J. Smart, Corporate Domicile and Multiple Incorporation in English Private International Law, Journal of Business Law 126 (1990); Lawrence Collins, 2 Dicey and Morris on The Conflict of Laws 1102-1103 (2000).

[41] See also Brigitte Knobbe-Keuk, Niederlassungsfreiheit: Diskriminierung- oder Beschränkungsverbot?, 51/52 DB 2573, 2578 (1990).

[42] See infra section VII.

[43] See supra note 17.

[44] See Schümann, supra note 13; Thönnes, 20 DB 1022 (1993).

[45] Eyles argues that where the head office is moved from Germany to Belgium, which does not require reincorporation but merely corporate adaptation to Belgian law, Germany should not dissolve the corporation but allow it to retain its legal personality in Germany until conversion/adaptation has been effected. See Uwe Eyles, Das Niederlassungsrecht der Kapitalgesellschaften in der Europäischen Gemeinschaft 334 (1990).

[46] See e.g. Bay. OLG of 7.5.1992–3 ZBR 14/92; and OLG Hamm, of April 30, 1997 (NJW-RR 1998, 615).

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corporation cannot relocate its head office and its registered office to Germany and, at the same time, retain its identity.[47] This rule appears to apply even where the state of departure does not require dissolution of the corporation, and where the arriving corporation adapts its statutes to conform to German law.[48] The same applies, for instance, in the Netherlands.

A. Different National Solutions

The national laws of several EU Member States provide various models for identity-preserving nationality changes. This is the case in Portugal and Italy, for example. In Portugal, which applies the *siège réel* theory, the Portuguese *Codigo das Sociedades Comerciais* (CSC) contains a model for identity-preserving nationality changes.[49] A corporation may be registered in Portugal and retain its legal personality if:

(1) the state of departure allows a transfer without dissolution, and
(2) the corporation adapts its statutes to conform to Portuguese law, and
(3) the corporation moves its registered office to Portugal by registration in Portugal.

If it does not comply with the registration requirement, the general rule in the CSC provides that the corporation is nevertheless bound by a contract concluded in Portugal. It is a consequence of the failure to register that the person(s) who concluded the contract as well as the management of the corporation are jointly and severally liable for the contractual obligation.[50]

A corporation registered in Portugal may also move its head office to another Member State despite the application by Portugal of the *siège réel* theory, provided, however, that the corporation changes its nationality. According to the CSC, Article 3.5, this change of nationality may be made without dissolving the corporation if the state of arrival allows an identity-preserving nationality change. To protect minority shareholders, the CSC provides that the resolution to change nationality shall be passed at a shareholder meeting by holders of at least 75% of the share capital. Furthermore, as long as it is registered in Portugal–irrespective of whether the head office is located in another state–the corporation may not claim as against third parties that it is governed by the law of another state.[51]

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[47] See OLG Zweibrücken 27.6.1990, reported in 6 IPRax 280 (1991); and Brigitte Knobbe-Keuk, 51/52 DB 2578 (1990). The courts appear to take the view that the decision to relocate the registered office also is a decision to liquidate the corporation, see e.g. Grossfeld and Boin's comment on Bay. OLG of 7.5.1992–3 Z BR 14/1992, Bernhard Grossfeld and Kai T. Boin, Anmerkung zu Cour de Cassation 12.11.1990, JZ 370, 372 (1993).

[48] See e.g. Steiger, supra note 25, at 53.

[49] Article 33.3 CSC.

[50] See Steiger, supra note 25, at 269. Moreover, the CSC provides that the courts may order that a corporation discontinue its business activities in Portugal and that the corporation's capital in Portugal be liquidated, provided the corporation has done business in Portugal for not less than one year and has its head office in Portugal but does not comply with the registration requirement.

[51] According to French law, which also applies the *siège réel* theory, the movement by a foreign corporation of its head office to France involves a change of nationality with the result that the foreign corporation must adapt to French corporate law, in particular the strict rules on disclosure in France, see

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Other EU Member States, such as Spain, Greece and Luxembourg, also make it possible to effect an identity-preserving nationality change. Luxembourg allows the registration of an arriving corporation without reincorporation, provided the statutes are adapted to conform to national law.[52] In 1994, the Netherlands introduced rules, which in case of "emergency" (war, revolution etc.), allow a Dutch corporation to effect an identity-preserving change of nationality if the state of arrival recognizes this.[53]

Some European countries that are not members of the European Union allow identity-preserving nationality changes. In Switzerland, a foreign corporation may move to Switzerland without reincorporation, provided (1) the state of departure allows an identity-preserving nationality change, and (2) the corporation can be adapted to the Swiss corporate form.[54]

IV. BACKGROUND TO THE FOURTEENTH EC COMPANY LAW DIRECTIVE

As already mentioned, the creation of the single European market is based on the condition that corporations are allowed to move from one Member State to another. *Prima facie* the relocation of corporations is regarded as a positive economic event. However, the European Parliament has especially pointed out that such transfers may also have adverse effects, such as socioeconomic problems in regions which corporations decide to leave.[55]

In order to realize the free movement of businesses, a comprehensive harmonization program covering, *inter alia*, corporate law matters has been initiated. The proposals dealing with corporate law matters have especially focused on facilitating cross-border cooperation and mergers between corporations. This has led to the adoption of the Regulation on the European Economic Interest Grouping.[56]

Ebenroth & Eyles, supra note 16, at 366. The question whether this change of nationality is identity-preserving if, without dissolution and reincorporation, the corporation adapts its statutes to comply with French law has not, as far as these authors are aware, been solved.

[52] See, e.g., Peter Behrens, Die Umstrukturierung von Unternehnem durch Sitzverlegung oder Fusion über die Grenzen im Licht der Niederlassungsfreiheit im Europäischen Binnenmarkt (Art. 52 und 58 EWGV), 1 ZGR 1, 10 (1994); Behrens, Identitätswahrende Sitzverlegung einer Kapitalgesellschaft von Luxenburg in die BRD, 8 RIW 590 (1986); and Ebenroth & Eyles, supra note 16. The same appears to apply in Belgium, see id.; Bernhard Grossfeld and Dieter Jaspers, Identitätswahrende Sitzverlegung und Fusion von Kapitalgesellschaften in der Bundesrepublik Deutschland, 53 RabelsZ 57 (1989); and Herbert Kronke, Deutsches Gesellschaftsrecht und grenzüberschreitende Strukturänderungen, 1 ZGR 26, 30 (1994).

[53] See Act of Oct. 13, 1994, Stbl. 1994, 800. Further on this Act, see Jaap Bellingwout, Motion: The KPMG Report 1993, *in* Wouters & Schneider, supra note 20, at 75.

[54] By adapting the bylaws so that they conform to the requirements set down in the Swiss Corporate Law pursuant to Articles 161 and 162 of the Bundesgesetz über das Internationale Privatrecht of December 18, 1987 (Federal Act on Private International Law). See further Grossfeld & Jaspers, supra note 52.

[55] See Resolution on Industrial Restructuring and Relocation in the European Union, 1996 O.J. (C 362) 147.

[56] See Regulation 2137/85, 1985 O.J. (L 199) 1.

Proposals for a Tenth EC Company Law Directive on cross-border mergers[57] and a Regulation on a European Company Statute (the so-called SE company)[58] have also been proposed. Moreover, a proposal for a Regulation on a private European limited company is being considered, but there is still no official proposal.[59]

So far, the European Commission has given little attention to the possibility of the individual corporation moving across borders. The provisions of the Regulation on the European Economic Interest Grouping and the proposal for an SE company, however, both anticipate that such corporate forms may be entitled to relocate the registered office.

The provisions of Article 293 of the EC Treaty also anticipate, to the extent necessary, the entry into negotiations with a view to securing "the retention of legal personality of companies in the event of transfer of their seat from one country to another." This provision sets the stage for the preparation of an international agreement making it possible for a corporation to move its registered office–in other words, a change of nationality. However, the content of such an agreement has never been under actual consideration.[60]

As mentioned in section II.D above, the judgment in the *Daily Mail* case demonstrated that, in some situations, problems arise when a corporation tries to conduct cross-border activities. The European Commission chose to cite the *Daily Mail* judgment in support of the requirement of further harmonization efforts in order to solve this problem. As a preliminary matter, the Commission asked the consulting and auditing firm KPMG to prepare a report on the subject. The report contained a proposal for two alternative solutions to ensure the improved mobility of corporations.[61] Both proposed solutions suggested partial harmonization of the conflict of laws rules of the Member States. In the first proposal, KPMG suggested a variant of the incorporation theory. In brief, it is suggested that a corporation should be free to transfer its head office from one Member State to another without resulting in a change of nationality and without the corporation having to be dissolved and reincorporated. The consequence of this solution is the abolition of the *siège réel* theory in all Member States. Consequently, this solution is unlikely to be adopted, as those Member States that apply the *siège réel* theory are not likely to abandon the *siège réel* theory at present. In the second proposal, KPMG provides a

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[57] The latest official proposal for a Tenth EC Company Law Directive is dated from 1985. See 1985 O.J. (C 23) 11. There already exists a new proposal from 1998 (internal doc. XVD2/6000/EN-REV7), and it is expected that it will soon become a new official proposal.

[58] See the latest official proposal 1991 O.J. (C 176) 1. There are further proposals for other European corporate forms (association, cooperative society and mutual society), see 1992 O.J. (C 99) 1.

[59] See Søren Friis Hansen, "Société fermée européenne" Et europæisk anpartsselskab i støbeskeen?, Julebog 187 (1998); and Peter Hommelhoff, Die Société fermée européenne, 1 Heidelberger Forum für Europäisches Recht, no. 104: Perspektiven des Rechts in der Europäischen Union–Die "Société fermée européenne" 47 (1998).

[60] As early as in the 1960s, the Commission commissioned the German professor Beitzke to prepare a report on the issue. An abridged version of this report was published in Günther Beitzke, Anerkennung und Sitztheorie von Gesellschaften, 127 ZHR 1 (1965).

[61] See European Commission publication of 1993: Study on transfer of the head office of a company from one Member State to another, carried out by KPMG European Business Centre, Brussels [hereinafter the KPMG Report]. The report is discussed by Bellingwout, supra note 53, at 75; Jaap Bellingwout, Die internationale Sitzverlegung juristischer Personen in Bewegung, 7 RIW 550 (1997).

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solution that solves the problem without forcing the Member States to apply a specific conflict of laws rule. The proposal does not allow restructuring by transferring the head office from and to states that apply the *siège réel* theory, in that the transfer of the head office will require a change of nationality. According to the proposal, company law rules should make it possible for a corporation to change its nationality without having to be dissolved in the state of departure and reincorporated in the state of arrival. The following discussion will show that the proposal for a Fourteenth EC Company Law Directive is based on the second proposal of KPMG.

V. THE PROPOSAL FOR A FOURTEENTH EC COMPANY LAW DIRECTIVE

In 1997 the European Commission presented an internal proposal for a Fourteenth EC Company Law Directive.[62] An Explanatory Memorandum supplementing the proposal and containing comments concerning the individual Articles was attached to the proposed Directive. References in the following text to the comments in the proposed directive are references to the Explanatory Memorandum.

According to Article 14 of the proposed Directive, the Member States have to implement their provisions not later than January 1, 2000. However, it must be assumed that serious discussions of the Fourteenth EC Company Law Directive will have to await the adoption of the Tenth EC Company Law Directive and the Regulation on the SE company. It is therefore reasonable to expect that it will be several years before the Fourteenth Directive is implemented.

A. The Solution to the Conflict of Laws Problem

Even though the Fourteenth EC Company Law Directive proposes to make it possible for a corporation to make an identity-preserving nationality change, the proposal does *not* harmonize the conflict of laws rules of the Member States. Consequently, Member States applying the *siège réel* theory still may require a corporation wishing to change its nationality to also move its *de facto* head office.

The fact that all Member States may retain their present conflict of laws rules clearly increases the chance of adopting the Directive, because the conflict of laws question is a politically sensitive issue in several Member States.[63] The Commission explicitly states that strict application of the principle of subsidiarity suggests that no attempt should be made to harmonize an area unless absolutely necessary.[64]

[62] See supra note 8.

[63] This is the case in certain countries applying the *siège réel* theory as well as certain countries applying the incorporation theory. See also Bellingwout, supra note 53, at 82.

[64] The principle of subsidiarity was introduced into Community law in 1992 and ensures that in areas which do not fall within the exclusive competence of the EU, it shall not take action unless the objectives of the proposed action cannot adequately be achieved by individual Member States. See further A.G. Toth, The Principle of Subsidiarity in the Maastricht Treaty, 29 C.M.L.R. 1079 (1992); Paul Demaret, A short Walk in the Realm of Subsidiarity, *in* European Economic and Business Law 13-32 (Richard M. Buxbaum, Gérard Hertig, Alain Hirsch & Klaus J. Hopt eds., 1996); and Denis J.

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The provisions of the Directive concerning the conflict of laws, however, give rise to a number of problems. The relevant provisions can be summarized as follows:

(1) Under Article 2, the registered office of a corporation is either the place where the corporation is registered, or the place where the corporation has its central administration and is registered.

(2) Under Article 11(2), the state of arrival may refuse to register an arriving corporation if its central administration is not situated in the state of arrival.

1. The Concept of "Central Administration"

The first of these problems is directly linked to the use in the proposed Directive of the concept of "central administration." The proposal does not specify the meaning of this concept. This raises the question whether the Directive seeks to harmonize the criteria for the physical connection between the corporation and the state applying the *siège réel* theory. If this is the case, then the question is rather: what does the concept of "central administration" actually mean. As mentioned in section II.A above, the uncertainty involved in the determination of the concept of "head office" in the individual Member States has resulted in significant problems, and these problems appear not to have been solved by the Directive. In relation to the Fourteenth EC Company Law Directive, doubts may therefore arise as to the necessary criteria for establishing that a corporation has relocated its central administration in connection with a change of nationality. To avoid such doubts, the Directive ought to have contained a definition of the concept of "central administration."[65]

2. Who Can Apply the *Siège Réel* Theory?

Article 11(2) of the proposal also gives rise to problems of interpretation. The provision entitles the state of arrival to enforce the *siège réel* theory by refusing to register the arriving corporation if it does not transfer its head office to the state of arrival at the same time. However, the proposal fails to address the consequences it may have if, after registration, the corporation again moves its head office to another state.

It is not clear either how a state of departure applying the *siège réel* theory may deal with a situation in which a corporation becomes registered in another country without moving its head office as well. This problem is highly relevant. For example, Germany may fear that German corporations will become registered in, for instance, the United Kingdom–and thereby become subject to the more flexible UK rules–while not moving their head office out of Germany. In such a case, the United

Edwards, Fearing Federalism's Failure: Subsidiarity in the European Union, 44 Am. J. Comp. L. 537 (1996).

[65] At least, rules of presumption making it easier to determine where a corporation has its central administration should be set forth.

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Kingdom, as the state of arrival, will not require that the German corporation transfer its head office to the United Kingdom, as the UK applies the incorporation theory. The question is then whether Germany, as the state of departure, may be entitled to enforce the *siège réel* theory, and if so, how.

It is clear from the Fourteenth EC Company Law Directive that it is not intended to harmonize the conflict of law rules. Accordingly, the Member States must still be entitled to enforce the *siège réel* theory, both as state of arrival and as state of departure. It is not clear, however, how this may actually be done. For example, the proposal does not open the possibility for Germany as a state of departure of refusing to delete the hitherto German corporation from the German register. Therefore, Germany does not appear (in this example) to be entitled to prevent the corporation from being re-registered as a UK corporation. But as it is now a corporation registered in the United Kingdom and has its head office in Germany, Germany ought to be entitled to declare the corporation a nullity by applying the *siège réel* theory.[66]

If it is assumed that a Member State may apply the *siège réel* theory to its full extent, it is open to discussion whether a state other than a state of departure or arrival is entitled to enforce the *siège réel* theory. For instance, is a Member State (A) entitled to declare a corporation a nullity if it has changed its nationality between two other Member States (B and C), and if the corporation has neither its registered office nor its *de facto* head office in the Member State (A)?[67] It would have been desirable if the proposed Directive had made it clear that the Member States are not entitled to enforce the *siège réel* theory in such cases.

3. Further Protection of Member States

Even though the Member States may enforce the *siège réel* theory, some countries may possibly find this to be insufficient to avoid the adverse effects that business relocations may have. Some Member States may fear that corporations change nationality in order to avoid certain corporate law rules, such as the rules on employee participation.[68] These Member States may still find that such relocations amount to circumvention, even though corporations move their *de facto* head office and change nationality at the same time.

This is the reason why Article 14(4) of Regulation on European Economic Interest Groupings provides that a state of departure may object to the decision of an Economic Interest Grouping to transfer its office to another Member State if the objection is based on grounds of public interest. Article 1(3) of the proposal for a Tenth EC Company Law Directive grants the Member States a similar right to refuse a cross-border merger if the result of such a merger would be that a merging

[66] Cf. the discussion of the German rules supra section II.B.2.

[67] Under German law, *inter alia*, a corporation will not be declared a nullity if the Member State in which the registered office and the state in which the *de facto* head office are located both take the view that the corporation is valid, because both states apply the incorporation theory. See Bernhard Grossfeld, Internationales und Europäisches Unternehmensrecht 41 (1995).

[68] Cf. the German fear of *Flucht aus der Mitbestimmung*.

corporation would "no longer meet the conditions required for employee representation in that undertaking's organs."[69]

A common feature of these reservations is that they permit a Member State as a state of departure to refuse to recognize cross-border activities if, as a result, the workers lose rights or if other public interest considerations may justify such refusal.[70] It seems likely that some Member States will demand the incorporation of a similar reservation in the Fourteenth EC Company Law Directive. It should be noted that, for instance, German authors have pointed out that the effects of incorporating such reservations could be to the disadvantage to German industry as it will not be able to fully benefit from the new opportunities of cross-border activities if Germany uses the reservation.[71] The Fourteenth EC Company Law Directive is therefore unlikely to be adopted until the question concerning employee participation has been settled.[72]

B. Which Corporations?

The Directive solely applies to corporations that have been incorporated in the EU Member States and change their nationality within the EU. Accordingly, a US corporation cannot rely on these rules and thus be converted into an EU corporation, unless such conversion is allowed under another set of legal rules.[73]

The existing Company Law Directives contain provisions specifying which corporate forms in the Member States fall within their scope of application, but the proposal for a Fourteenth Directive of November 11, 1997 specifies its scope thus:

> However, this Directive will cover not only public limited companies but also other companies with share capital.[74]

It was intended by the first draft of April 20, 1997 that it should govern all corporate forms. By the second draft of November 11, 1997, the scope has been restricted to corporations with limited liability.[75] However, the wording of the Directive may give rise to problems of interpretation. The Directive evidently governs the two corporate forms, public limited company and private limited company.[76] It is more difficult to determine whether other corporate forms with limited liability fall within the scope of the Directive, as they have limited liability

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[69] Tenth EC Company Law Directive, supra note 57, Article 1(3).

[70] In this connection it is pointed out that the Merger Taxation Directive allows a Member State to refuse to grant tax benefits to a cross-border merger, division, transfer of assets, or exchange of shares that has as its principal objective tax evasion or tax avoidance, or where the merger has as a result that the employees lose their right to be represented in management. Cf. Article 11(1), Council Directive 90/434/EEC, 1990 O.J. (L 225) 1.

[71] See the arguments put forward in Eyles, supra note 45, at 220 (1990).

[72] See further infra section VI.

[73] For instance, on the basis of a treaty; further on this subject, see the treaty between Germany and the United States mentioned in note 17 supra.

[74] See Proposed Fourteenth EC Company Law Directive, supra note 8.

[75] Below, the members of a corporation are referred to as shareholders, regardless of whether they are termed differently in some corporate forms.

[76] See supra note 5.

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but no "share capital" in the proper sense of the term. This problem is currently being considered by the European Commission.

Typically, a corporation changing its nationality is likely to be incorporated in the state of arrival in the corporate form most closely resembling the corporate form it had in the state of departure. Thus, a French *Société Anonyme* (SA) wishing to move to Germany will most properly be incorporated as a German *Aktiengesellschaft* (AG), and a French SARL as a German GmbH. However, this is not specifically required in the Directive. It appears from the comments in the Explanatory Memorandum that, if there is no corresponding corporate form in the state of arrival, the Directive requires a change of nationality to be combined with the rules regulating changes between corporate forms. This also appears to apply where, in connection with a change of nationality, a corporation wants to adopt a corporate form other than the corresponding corporate form in the state of arrival. According to the comments, it is up to the corporation to find an appropriate solution to this problem and to indicate it in the transfer proposal. It must be assumed, however, that it will depend on the national laws which requirements have to be complied with to effect a corporate conversion.

It finally follows from Article 13 that a corporation may not change its nationality if bankruptcy or liquidation proceedings have been commenced.

C. The Procedure for Nationality Change

Under the proposed Fourteenth Directive, the change of nationality of a corporation is initiated by the preparation and publication by the management of a transfer proposal, which shall indicate:

(a) the proposed new registered office;
(b) the corporate form that the corporation will adopt;
(c) prepared new statutes that conform to the law of the state of arrival and, where appropriate, the new name of the corporation;
(d) a proposed transfer timetable. [77]

In addition, the management of the corporation has to prepare a report explaining and justifying the implications of the transfer for shareholders and employees.[78]

No decision to effect the transfer may be taken for two months after publication. The decision to transfer must be adopted by a majority of not less than two-thirds of the votes cast at a shareholders' meeting,[79] subject to special rules having to be laid down if a corporation has several categories of shareholders.[80]

In the state of departure, the compliance with the above-mentioned rules has to be supervised, but it is for the Member States to decide whether this is to be done by

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[77] Id., Article 4.

[78] Cf. id., Article 5.

[79] Alternatively, the Member States may stipulate that a quorum is present when half the share capital is represented and when not less than a simple majority votes to adopt the proposal. Cf. id., Article 6(3).

[80] See further infra section V.D.

judicial or administrative supervision. A certificate conclusively attesting to the completion of the pre-transaction acts and formalities must be issued.[81] When the certificate has been issued, a new registration in the state of arrival may be effected; this registration has to be effected within 30 days of the issuance of the certificate.[82] A state of arrival may refuse to register a corporation if evidence is not produced that the central administration also has been moved to the state of arrival.[83]

The new statutes and the change of nationality are effective from the date on which the new registration is made.[84] Once registration has been effected, the old (previous) register must be informed of this, and not until this happens may the corporation request that the entry in its regard be deleted from the old register. The new registration has to be made public in both Member States concerned. Until such publication is made, third parties may rely on the old registration unless such third parties are aware of the new registration.[85]

D. Minority Shareholder Protection

A decision to move the corporation to another Member State may negatively affect minority shareholders. By changing its nationality, the corporation becomes subject to a new legal system, and thereby the minority shareholders lose the minority guarantees ensured by the law of the state of departure. They also become subject to the rules on minority protection of the state of arrival. Indeed, one of the arguments for the *siège réel* theory is that shareholders ought to be entitled to rely on the protection afforded by the law of the state in which the corporation conducts its activities.[86] Even though some harmonization of corporate law has today been achieved, it is true that the differences between the rules on minority shareholder protection in the EU Member States still are substantial[87] so that the protection of minority shareholders warrants particular consideration in the event of a change of nationality.[88] Moreover, because the Fifth EC Company Law Directive (Structure Directive) has not been adopted, several of the rules on the legal rights of shareholders have not been harmonized. In relation to other forms of business

[81] Cf. Proposed Fourteenth EC Company Law Directive, supra note 8, Article 9.

[82] Cf. id., Article 10.

[83] Cf. section supra V.A.

[84] Cf. Proposed Fourteenth EC Company Law Directive, supra note 8, Article 11(1).

[85] Cf. id., Article 12.

[86] A potential investor resident in the state of departure should obviously not be taken into consideration. Such investor is free to choose whether he wants to acquire a minority holding in a foreign corporation and thus become subject to foreign corporate law.

[87] This argument cannot be cited in support of the application of the *siège réel* theory instead of the incorporation theory. Where a corporation chooses to move its head office to another Member State, the result will be a change of nationality in the state of departure if this state applies the *siège réel* theory. In contrast, this will not be the case if the state of departure applies the incorporation theory and therefore, the interests of the minority shareholders may be said to speak in favor of the incorporation theory and against the *siège réel* theory, see e.g. KPMG report, supra note 62, at 19.

[88] This consideration does not justify, and never has, a requirement for the dissolution of the corporation on a change of nationality, see Kruse, supra note 13, at 180. If, for instance, all shareholders vote for a change of nationality, the interests of the minority may not justify dissolution, because the minority shareholders have voluntarily waived this option.

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entities, harmonization efforts have not even been proposed. The current minority guarantees afforded by the individual Member States therefore differ considerably.

The Fourteenth Directive requires that rules on the protection of minority shareholders be laid down, but according to Article 7, it is for each Member State to adopt provisions specifying the contents of such protection.

Different models for the protection of minority shareholders in connection with a change of nationality may be envisaged. One model protects minority shareholders by introducing a requirement for unanimity, thus giving each shareholder a right to veto the decision. A requirement for unanimity as a means to protect minority shareholders is not the optimum solution, however, if a change of nationality is intended to be practically possible.[89] Unanimity may be reached in small corporations with few shareholders, but in large corporations, for instance those listed on a stock exchange, it will be virtually impossible to reach unanimity.

Another method for safeguarding the interests of minority shareholders is to introduce an exit option for minority shareholders. This was obviously the solution which the European Commission had in mind.[90] It may be envisaged that the resolution has to be passed by a qualified majority, for instance two-thirds, or perhaps even nine-tenths, of the votes cast and of the voting share capital represented at the shareholders' meeting. The shareholders who opposed the decision for a change of nationality may then demand a repurchase of their shares. The appraisal remedy is also found in the US rules on mergers, which give the dissenting shareholders a right to demand payment of the fair value of their shares.[91] The appraisal remedy may provide the basis for a balanced model for a change of nationality; on the one hand, a change of nationality is made possible, whereas on the other hand, minority shareholders are protected from being forced to become subject to another jurisdiction.

One argument against repurchase provisions obviously is that a shareholder already has an exit option when the shares are transferable. As for listed corporations, the right to sell shares is a key right for shareholders who want to extricate themselves from the corporation, but there hardly is a market for shares of unlisted corporations, especially not for minority holdings of a corporation in the process of changing its nationality. If, exceptionally, a minority shareholding can be sold, it is unlikely that the shareholder will get a price equivalent to the net value of the corporation. Accordingly, the right of transfer is not an appropriate solution if genuine protection of minority shareholders is desired.

The repurchase model does not, however, solve all problems. The (directive-based) rules of the Member States on the acquisition by a company of its own shares, as well as the rules on capital reduction, are likely often to restrict the practical possibility of effecting a change of nationality.

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[89] For the same reason, the proposal for a Tenth EC Company Law Directive explicitly states that the Member States may not require a larger majority for cross-border mergers than they require for national mergers. This was done in order to ensure that Member States did not make the possibility of cross-border mergers illusory.

[90] Cf. the comments on Article 7 of the Proposed Fourteenth EC Company Law Directive.

[91] See e.g. Cox, Lee Hazen & O'Neal, supra note 2, at 595.

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According to the Second EC Company Law Directive on capital requirements, the corporate laws of the Member States may allow corporations to acquire not more than 10% of their own shares–i.e. shares of a nominal value equivalent to 10% of the nominal share capital.[92] The Directive further requires that shares may only be acquired out of the distributable reserves of the corporation. These rules result in substantial restrictions on the acquisition by a corporation of its own shares.

If it is necessary for a corporation to acquire more than 10% of its own shares, the acquisition may only be made in connection with a reduction of the share capital. According to the provisions of the Second EC Company Law Directive, there must be funds to fully cover the share capital after the reduction of capital.

Because of the restrictions that the rules on the acquisition of own shares and capital reduction impose on the duty to repurchase shares in connection with the capital reduction of a corporation, consideration may be given to the introduction of a provision to the effect that the remaining shareholders are required to purchase the shares of the minority shareholders if the corporation is unable to complete the repurchase.[93] Without such provision, the problem may, however, be solved practically by first reducing the share capital and then increasing the capital by an equivalent amount (contributions from other persons than those from whom shares have been acquired). Even though these solutions are possible, there hardly can be any doubt that the rules on the repurchase of shares and capital reduction will be obstacles to the decision to change nationality; particularly for small and medium-sized corporations with only the required minimum capital. In such cases, a change of nationality will require that the shareholders who want to effect the change of nationality will have to "pay up" if minority shareholders demand a repurchase.

A third possible solution in the event of a change of nationality is that the legislators find such change to be one of the operational decisions that minority shareholders have to accept. In connection with a merger of corporations, minority shareholders may not demand a repurchase of their shares pursuant to the Third EC Company Law Directive on mergers.[94] A merger requires the approval of a simple majority or a qualified majority in the discontinuing corporation depending on the national laws involved, regardless of whether the shares of the new corporation are subject to, for instance, restrictions on transfer. The minority shareholders have to accept that their shares of the discontinuing corporation are exchanged for shares of the continuing corporation. In many respects, a merger may be likened to a change of nationality, so that it would therefore be logical to choose the same model of protection of minority shareholders.

In addition to the question of minority protection, another highly relevant problem may arise. If a class enjoys special rights, it may be difficult to grant similar rights after a change of nationality, because the corporate law rules of the state of

[92] See Articles 19-22 of Directive 77/91, 1977 O.J. (L 26) 1. For a detailed discussion of the rules in the Directive on own shares, see Werlauff, supra note 6, at 160. As the laws governing private limited companies are not subject to harmonization in the Second EC Company Law Directive, the Member States are free to choose whether or not to allow the acquisition of own shares in this type of corporation.

[93] Another solution would be to exempt the repurchase of own shares as part of a change of nationality from the rules against acquiring more than 10 percent of own shares.

[94] See Directive 78/855, 1978 O.J. (L 295) 36.

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arrival may not recognize this type of special rights. One example of this is where the share capital is divided into classes with different voting rights. Some countries recognize unlimited differentiation of the voting rights of shares (as in the UK), or more or less limited differentiation (as in the Nordic countries, which recognize differentiation of not more than a ratio of 10:1).[95] A number of Member States do not recognize differentiation in voting rights to the same extent. As an example, Spain and Italy apply an equality principle that does not allow differentiation of voting rights. In other countries, such as Germany, differentiation of voting rights is unlimited but only for 50% of the share capital at the most. This also applies to listed corporations in the Netherlands.

One result of these very divergent rules on differentiation of voting rights is that if, for instance, a Danish corporation allowing different voting rights wants to change to a Spanish corporation, this difference in voting rights has to be abandoned. In order to protect shareholders whose class rights are significantly affected by a change of nationality, the proposal for a Fourteenth EC Company Law Directive provides that the decision to change the nationality of a corporation with several classes of shares has to be adopted separately by each class of shareholders.[96]

E. Protection of Creditors

As a change of nationality merely means that the artificial person becomes subject to another legal system while retaining its legal personality, a change of nationality does not *prima facie* involve a change of debtor. Therefore, the creditors do not have to approve the change of nationality.

The question is whether the change of nationality may be deemed to have such consequences for creditors and contracting parties that they nevertheless are entitled to some form of protection.

The change of nationality involves the transfer of the registered office, and thus jurisdiction, of the corporation; and after the transfer, the corporation generally has to be sued in the state of arrival.[97] As the corporation typically continues to conduct activities in the state of departure, it is likely that, in practice, there will often be a branch that is subject to the jurisdiction of the state of departure, and thus the creditors may still sue the corporation in their own country.

The change of nationality by a corporation does not generally affect the law governing the relationship between the corporation and its creditors, or between the

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[95] Thus, no harmonization of the rules on voting rights has been made; though a proposal for the harmonization of the rules governing public limited companies exists. The basis of the proposal for a Fifth EC Directive is that all shares should carry equal rights, cf. Article 33(1). However, Article 33(2) provides: "Notwithstanding paragraph 1, the laws of the Member States may authorize the memorandum and the articles of association to allow restriction or exclusion of the right to vote in respect of shares which carry special pecuniary advantages. Such shares may not be issued for an amount exceeding 50% of the subscribed capital." The Directive further provides that when the corporation has not fulfilled the obligations in respect of such special pecuniary advantages, the differentiation of voting rights will lapse.

[96] Cf. Article 6.

[97] See Article 2 compared with Article 53 of the Brussels Convention from 1968 (Convention of 27 September, 1968, on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters). All EU Member States have acceded to this Convention.

corporation and its business associates. The law applicable to a contract will often have been chosen by the parties and will therefore not be changed as a result of the change of nationality. To the extent that the parties have not chosen the law applicable to the contract, the applicable law will depend on the residence/domicile of the parties at the time when the contract was concluded. Any subsequent change of nationality and thus a transfer of the registered office by the corporation is immaterial.[98]

If a creditor has a claim secured on real or personal property, the change of nationality by the owner will not affect the validity of the security interest. On the other hand, the question of whether the acts of perfection of one or the other state have to be complied with may be directly affected by the physical movement of the security to another Member State.[99] If the claim is secured on the corporation itself, as in the case of a floating charge under UK law, the property given as security is moved as a result of the change of nationality; and therefore, the security interest may be lost unless re-registration is made. Similarly, problems may arise for holders of corporate bonds in the case of a change of nationality.

The fact that a corporation becomes subject to the law of another Member State may also affect the creditors insofar as they are protected by corporate law rules. As an example, if a Swedish corporation changes its nationality and corporate form to a UK private limited company, the result will be that new rules on capital requirements and capital protection apply.[100] Creditors may therefore find that their interests have been prejudiced.[101]

As it may be difficult to determine exactly whether the rights of creditors are prejudiced, the proposed Directive has opted for the simple solution of protecting all creditors. Under Article 8, the creditors and holders of other rights in respect of a corporation may require the corporation to provide adequate security for their debts. All creditors whose debts were incurred before publication of the transfer proposal may require such guarantee. However, a Member State may, if so desired, extend this arrangement to a corporation's debts to public bodies incurred up to the date of the actual change of nationality.[102]

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[98] See Peter Stone, The Conflict of Laws 244 (1995); and Allan Philip, EU-IP 146 (1994) in relation to the Rome Convention of 1980 (Convention on the law applicable to contractual obligations). This Convention regulates most questions concerning the choice of applicable law to contracts and applies in all EU Member States.

[99] See e.g. Stone, supra note 98, at 363 on English law; Arnt Nielsen, International privat- og procesret 619 (1997) on Danish law; and Gerhard Kegel, Internationales Privatrecht 574 (1995) on German law.

[100] For instance, there is no minimum capital requirement for a UK private limited company, whereas the minimum requirements in Sweden are among the highest in the EU. This raises the question whether, for example, it may be required that a Swedish corporation necessarily has to maintain the same share capital on its conversion to a UK private limited company, or the share capital may be reduced as part of a change of nationality. The proposal fails to address this issue, but it must be presumed that the corporation must (also) comply with the rules of the state of departure regulating the reduction of capital in connection with a change of nationality if this change in effect is a reduction of capital.

[101] See also Grossfeld, supra note 67, at 85.

[102] Cf. Proposed Fourteenth EC Company Law Directive, supra note 8, Article 8(2).

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The effect of the chosen solution is that it becomes more expensive for a corporation to change nationality. In consequence, only clearly solvent corporations have this possibility, but this was probably also the intention. A number of practical problems, however, may arise as to determining what actually constitutes adequate security. Apart from these objections, the solution has the distinct advantage of fully protecting the creditors against a corporate restructuring, the consequences of which the creditors may only be able to fully recognize with difficulty.

VI. PROTECTION OF EMPLOYEES

The proposed Directive provides that in cases where employees are represented on the governing bodies of the corporation prior to the change of nationality, the transfer proposal must state how employee involvement is to be effected after the transfer.[103] The proposal states, however, that this part of the provision will be finalized in the light of the outcome of the discussions on the Davignon Report. The Davignon Report is the name of a report on employee participation that was prepared by a group of experts in 1997.[104]

The Davignon Report addresses one of the greatest obstacles to the adoption of the Directive, the question of employee participation.[105] The harmonization of the rules on the right of employees to be represented in the corporation has now been discussed for nearly 30 years. The discussion originally started in connection with the first proposal for a Fifth EC Company Law Directive of 1972. The question is, however, particularly relevant in respect of the corporate law proposals ensuring the right of corporations to conduct cross-border activities, including merger, transfer of registered office, etc.[106] Certain countries–notably Germany–fear that corporations will try to escape from the rules on employee participation through merger or by moving out of the country, i.e. the so-called "flight from codetermination." When harmonizing the rules, it must be ensured that the employees have a right of some form of representation in all Member States before corporations are allowed to take such cross-border initiatives. This question also is relevant in connection with the Fourteenth EC Company Law Directive because some countries may fear that corporations change nationality for the sole purpose of avoiding employee participation in management.

However, other countries do not want employee participation at all, and it has so far proven impossible to implement any harmonization of the rules. The Davignon

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[103] Cf. id., Article 4.

[104] Final Report of the Group of Experts on European Systems of Worker Involvement (with Regard to the European Company statute and other pending proposals), May 1997, <http://europa.eu.int/comm/employment_social/soc-dial/labour/davignon/davi_en.htm> (visited July 21, 2000).

[105] See also Hans-Werner Neye, Anmerkung, 39 ZIP 1697 (1997), who is of the opinion that the Member States will soon reach a consensus as to the content of the Fourteenth EC Company Law Directive, except as to the problem concerning employee participation.

[106] For recent literature on this subject, see e.g. Klaus J. Hopt, Labor Representation, *in* Buxbaum et al., supra note 64, at 241; Manfred Weiss, Worker Participation in the European Union, *in* European Community Labour Law: Principles and Perspectives 213 (Poul Davies et. al. eds., 1996); Karsten Engsig Sørensen, Harmoniseringen af aktieselskabers struktur, *in* Selskabers organisation 91, 221 (Paul Krüger Andersen ed., 1997).

Report recommends the laying down of rules on employee participation in the SE company. Even though the report does not explicitly propose a solution applicable to corporations other than the SE company, it clearly intends to establish a basis which will make it possible for "ordinary" national corporations to conduct cross-border activities in the long term.

VII. FISCAL CONSEQUENCES

Another unsolved problem is the effect of tax law incidental to a change of nationality. This problem was examined in the *Daily Mail* case, which in reality is a tax case, even though the focus was on the consequences of the *siège réel* theory.[107] The judgment made it clear that it is not contrary to the rules on the freedom of establishment in the Treaty of Rome if a Member State treats a complete liquidation of a corporation as a taxable event and imposes a tax on gains when the corporation moves its head office to another country, with the result that the corporation becomes fully liable to pay tax in the new state.

Member States are unlikely to have rules regulating the fiscal consequences of a change of nationality for the simple reason that a change of nationality is not always possible at present. Several countries, however, treat a transfer of the head office of a corporation as a taxable event equivalent to a complete liquidation of the corporation. Consequently, the existing rules become yet another obstacle to the mobility of corporations, and also in this respect is the EU different from the United States.[108]

In order to ensure an actual possibility of effecting a change of nationality, the Commission calls for the relevant tax laws to be harmonized.[109] It is emphasized that the solution is to be equivalent to the solution chosen in the Merger Taxation Directive on cross-border mergers, divisions, etc.[110] One effect of this solution will be that, generally, neither the corporation nor the shareholders will be liable to pay a tax charge as a result of a change of nationality. A tax charge will only be imposed if assets are physically moved out of a Member State.

VIII. THE CONSEQUENCES OF THE PROPOSED DIRECTIVE

The foregoing discussion shows that there still are many issues, in particular concerning tax and employee participation, which need to be resolved before the adoption of the Fourteenth EC Company Law Directive is likely. If it is assumed that these issues are resolved, it raises the question as to which consequences may be expected as a result of the adoption of the Directive.

First, the provisions governing the change of nationality in the Fourteenth EC Company Law Directive clearly introduce an innovative concept into the laws of

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[107] Cf. supra section II.D.

[108] See Romano, supra note 2, at 133.

[109] See comments, supra p. 9.

[110] See Directive 90/434, 1990 O.J. (L 225) 1. The Merger Taxation Directive is discussed, *inter alia*, in Ben Terra and Peter Wattel, European Tax Law 265-284 (1997); and Paul Farmer and Richard Lyal, EC Tax Law 277-292 (1994).

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several Member States, including the Nordic countries (Sweden, Finland, Denmark, and Norway), which do not have any current rules on corporate change of nationality.[111] The same is true for the United Kingdom.[112] As stated in section III above, a number of countries have rules on the change of nationality, but these national rules have not been coordinated with the national rules of other Member States. The implementation of the Fourteenth EC Company law Directive will therefore result in an increased mobility of corporations within the European Union.

Some Member States may fear that the result of this increased mobility will be competition between Member States to attract corporations as it has been seen in the United States. There is however no reason to assume that one EU Member State will eventually become a European "Delaware."

One consequence of the harmonization of minimum standards is that–in particular concerning public limited companies–many rules are applied in all the Member States and cannot therefore be "avoided" by a change of nationality. The question is whether the existing harmonization is sufficient to completely rule out competition among Member States in formulating corporate rules. As is apparent from the discussion in section VI above, it is possible to argue for harmonization of the rules on employee participation in order to prevent "flight from codetermination;" otherwise competition among Member States regarding this issue may result. To avoid such competition, it may also be necessary to harmonize in other areas, *inter alia*, the rules on shareholders' voting rights, the protection of minority shareholders, and the duties and liabilities of directors.[113]

Second, the continued application of the *siège réel* theory will also reduce the risk of a European Delaware effect. As many countries still apply the *siège réel* theory, corporations also normally have to relocate their head office in order to change nationality. Therefore, a change of nationality often is, in reality, a business transaction and not just something done *pro forma*.[114] The continued application of the *siège réel* theory may, however, restrict the possibility for corporations of exercising the right to change nationality under the Fourteenth EC Company Law Directive in practice. There still are considerable doubts about the definition of the concept of "head office," and this may create legal uncertainty for corporations with many international activities. Another type of uncertainty arises in those Member States that have not decided whether to apply the *siège réel* theory or the incorporation theory. This is the case in, for instance, Norway, where legal scholars do not agree on which conflict of laws rules apply, and where neither statutory law nor case law has solved the question.[115]

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[111] See Mette Neville & Karsten Engsig Sørensen, Selskabers nationalitetsskifte, 1 Nordisk Tidsskrift for Selskabsret 37 (1999).

[112] See David Lewis, Corporate redomicile, 16 The Company Lawyer 295 (1995); and Cheffins, supra note 3, at 427-428.

[113] See Clark D. Stith, supra note 2, at 1593-1597 (1991); and David Charney, Competition Among Jurisdictions in Formulating Corporate Law Rules: An American Perspective on the "Race to the Bottom" in the European Communities, 32 Harv. Int'l L. J. 423 (1991).

[114] For some corporations, including many mutual funds and other financial corporations, it will clearly be relatively easy to move the corporate head office to another country, because the management does not have to meet very often and therefore, the occasional business trip is sufficient.

[115] See Neville & Engsig Sørensen, supra note 111, at 37.

Third, there are no fiscal advantages of becoming the Delaware of the European Union. The main reason for the competition among states in the USA was the potential for increased tax revenue; in the EU, we do not impose an annual franchise tax and therefore, the motivation of the individual Member States for attracting corporations is not as high in the EU.[116] If a Member State wants to lower its corporate income tax rate to attract corporations from other countries, it may be prevented from doing so by the new EU policy that aims at discouraging harmful tax competition among Member States.[117]

Even if the Fourteenth EC Company Law Directive is adopted, there will still be substantial differences between the rules allowing corporate migration in the EU compared to the present situation in the USA. It is to be expected that the possibility of changing nationality will only result in very limited competition among Member States in formulating corporate rules, and a change of nationality will often have to involve an actual transfer of the corporate activity because of the wide application of the *siège réel* theory.

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[116] See Romano, supra note 2, at 133; and Cheffins, supra note 3, at 435-436.

[117] On December 1, 1997, the Ecofin Council adopted a Code of Conduct for Business Taxation, 1998 O.J. (C 2) 1, which commits the Member States (politically) to abolish tax schemes which reduce the tax burden to attract foreign direct investment. This political commitment is supplemented by the rules on unlawful state aids found in the EC Treaty, and which may also prevent such tax competition. See Carlo Pinto, EU and OECD Ought to Fight Harmful Tax Competition: Has the Right Path Been Undertaken, 26 Intertax 386 (1998).

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