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EUROPEAN COURT PRACTICE ON THE FREEDOM OF SETTLEMENT OF COMPANIES WITHIN EUROPEAN UNION

Summary

The approximation to the acquis communautaire of the European Union is the main field of interest for the legal reformers in South East Europe to complete their efforts to join the European Union. Next to the legal acts of primary and secondary legislation of the European Union court practice of the European Court of Justice had and has a deep impact on both, the legal practice and the legislation in member states. Here the court practice with regard to the freedom of establishment of companies will be described and reflected to the legal development in South East Europe. Remarks will be given to reflect this year topic of the Annual Meeting of the Business Lawyers Association "Economy and Legal Responsibility".

The contribution is based on lectures, given at the Faculty of Economics and the Faculty of Law at the University of Belgrade.

Key words: *European company law, European Court of Justice, acquis communautaire, freedom of establishment.*

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I European Company Law

With the Lisbon Treaty numbering and even the name of the basic contracts, establishing the European Union, were changed, but the primary legislation with respect to companies remain the same. With respect to companies in the Treaty on the Functioning of the European Union[1] Article 49[2] and 54[3] are to be taken into account:

> "Article 49
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> Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.
>
> Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the Chapter relating to capital."
>
> "Article 54
>
> Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Union shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States.
>
> 'Companies or firms' means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making."

Starting point for European secondary legislation was the first directive on Company Law, which is dated from 1968[4]. This documents the importance

1 Former Name: Treaty Establishing the European Community.

2 Former numbering Art. 43.

3 Former numbering Art. 48.

4 First Directive of the Council from March 9th 1968 an coordination of protection measures, which are zur Koordinierung der Schutzbestimmungen, die in den Mitgliedstaaten den Gesellschaften im Sinne des Artikels 58 Absatz 2 des Vertrages im Interesse der Gesellschafter sowie Dritter vorgeschrieben sind, um diese Bestimmungen gleichwertig zu gestalten (68/151/EWG), zuletzt geändert durch die Richtlinie 2003/58/EG des Europäischen Parlaments und des Rates, L221, 13 (Publizitätsrichtlinie).

of cross boarder handling of companies, since with this directive the very first directive on civil law at all was made by the European Community. May to document the early stage of legislation shortly after enactment of the first directive on company law two international treaties[5], signed by the Member States of European Community were agreed but never ratified.

Up to 2004 another 10 directives were enacted, which had different impact on legislation in member states. While the first directive initially only reflects the state of the arts in German legal practice[6] e.g. the Directive on Accounting[7] led to deep changes in systematic and content of German Company Law[8]. Since we want to focus on the impact of court practice, here the main directives are only listed, which are:

- First Council Directive 68/151/EEC of 9 March 1968 on co-ordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community (*OJ L 65*, 14.3.1968, p. 8–12). Replaced by Directive 2009/101/EC of 16. September 2009
- Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent (*OJ L 26*, 31.1.1977, p. 1–13). Last amendment by 32009L0109 of 22. October 2009
- Third Council Directive 78/855/EEC of 9 October 1978 based on Article 54 (3) (g) of the Treaty concerning mergers of public limited liability companies (*OJ L 295*, 20.10.1978, p. 36–43). Last amendment by 32009L0109 of 22. October 2009

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5 BULL. SUPPL. NO 2-1969 P. 7-14; Protocol on the agreement on mutual acknowledge of companies and legal persons BULL. SUPPL. NO 2-1969 P. 15-16. The second treaty was on cross boarder merging of joint stock companies, where a German version can be found in RabelsZ 39 (1975), 539ff.

6 Only fine tuning had to be done with respect to selected information on business papers. With the amendments in directive 2003/58/EC, the German system of publication within paper registers had to be changed dramatically, see Wolfgang Kilian, Europäisches Wirtschaftsrecht (European Business Law), Munich 2008, Marginal Number (MN) 587.

7 OJ L 222, 14.8.1978, p. 11–31.

8 See Kilian (FN 7), MN 593, Mathias Habersack, Europäisches Gesellschaftsrecht (European Company Law), Munich 2003, MN 266.

- Fourth Council Directive 78/660/EEC of 25 July 1978 based on Article 54 (3) (g) of the Treaty on the annual accounts of certain types of companies (*OJ L 222*, 14.8.1978, p. 11–31). Last Amendment by 32009L0049 of 16. July 2009
- Sixth Council Directive 82/891/EEC of 17 December 1982 based on Article 54 (3) (g) of the Treaty, concerning the division of public limited liability companies (*OJ L 378*, 31.12.1982, p. 47–54). Last amendment by by 32009L0109 of 22. October 2009
- Seventh Council Directive 83/349/EEC of 13 June 1983 based on the Article 54 (3) (g) of the Treaty on consolidated accounts (*OJ L 193*, 18.7.1983, p. 1–17). Last amendment by 32009L0049 of 16. July 2009
- Eighth Council Directive 84/253/EEC of 10 April 1984 based on Article 54 (3) (g) of the Treaty on the approval of persons responsible for carrying out the statutory audits of accounting documents (*OJ L 126*, 12.5.1984, p. 20–26)
- Eleventh Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State (*OJ L 395*, 30.12.1989, p. 36–39)
- Twelfth Council Company Law Directive 89/667/EEC of 21 December 1989 on single-member private limited-liability companies (*OJ L 395*, 30.12.1989, p. 40–42). Replaced by Directive 2009/102/EC of 16 September 2009 (*OJ L 258*, 1.10.2009, p. 20–25)
- Directive 2004/25/EC of the European Parliament and of the Council of 21 april 2004 on takeover bids (*OJ L 142*, 30.4.2004, p. 12–23)
- Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies (*OJ L 310*, 25.11.2005, p. 1-9). Last Amendment 32009L0109 of 22/10/2009
- Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies (*OJ L 184*, 14.7.2007, p. 17–24).

Next to directives, European Union starts to enact regulations on Company Law to introduce special European forms of companies[9]. While the

9 With two other regulations, International Accounting Standards became binding all over Europe. Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards (*OJ L 243*, 11.9.2002, p. 1–4); Commission Regulation (EC) No 1725/2003 of 29 September 2003 adopting certain international accounting standards in accordance with Regulation (EC)

first approach with the Regulation on European Economic Interest Group[10] had only limited impact within Europe[11] with the Societé European[12] a form was established, which is accepted in the European business practice[13].

It has to be stated, that European Company Law does not tries to unify Company Law regimes in the member countries but to simplify cross boarder activities between the member states[14]. Nevertheless had the European secondary law deep impact on the legislation and legal practice in member states. The same is true and even from more interest, for the impact by decisions of the European Court. Different as in legislative activities, where the directives and in particular regulations are result of, partly long-lasting discussions[15], member states are not involved in the court practice. Even when this practice only concretized European primary law, as stated in Art. 49 and 54 of the Treaty on the Functioning of the European Union, it will be shown, that also this has a direct impact not only on the legal handling of cross boarder cases but also on the legislation in member states.

II European Court Practice on the Right of Establishment

1. Daily Mail

Starting point of the European Court practice on the freedom of establishment as stated was the Daily Mail Decision[16]. In that case the Daily Mail and General Trust PLC want to remove its seat from Great Britain to

No 1606/2002 of the European Parliament and of the Council (*OJ L 261*, 13.10.2003, p. 1–420).

10 Council Regulation (EEC) No 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG) (*OJ L 199*, 31.7.1985, p. 1–9).

11 The same is true for the European Cooperative Society (Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society (SCE), (*OJ L 207*, 18.8.2003, p. 1–24)), see Marcus Geschwandtner, Marcus Helios, „Neues Recht für die eingetragene Genossenschaft (New Law for the registered cooperative society)", *Neue Zeitschrift für Gesellschaftsrecht (NZG)*, 2006, 691.

12 Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE) (*OJ L 294*, 10.11.2001, p. 1–21). Last amendment by 32006R1791 (*OJ L 363*, 20.12.2006, p. 1–80).

13 See e.g. *http://www.handelsblatt.com/unternehmen/aussenwirtschaft/societas-europaea-eine-gesellschaftsform-mit-zukunft;1440875*, Noelle Lenoir, „The Societas Europea (SE) in Europe – A promising start and an option with good prospects", *Utrecht Law Review*, 2008, 13 (*http://www.utrechtlawreview.org/publish/articles/000057/article.pdf*).

14 See Killian (FN 7), MN 584; Habersack (FN 9), MN 24.

15 Societe europeae was started to be discussed in the 1970's but only enacted in 2001, see Killian (FN 7), MN 620.

16 C-81/87, European Court reports 1988 Page 05483.

the Netherlands, not at least, to prevent taxes, since it was planned to sell assets and to buy own shares from the fund gathered. Under British Tax Law, a corporate, subject for corporate income tax in Great Britain needs for domicile move approval by the treasury. That approval was denied and Daily Mail asked the British court for abolishment of that decision and allowance to move to Netherlands. They argued that the need for an approval violate their rights, arising from Art. 52 and 58 of the Treaty on Establishment of the European Community (now 49 and 54 of the Treaty on the Functioning of the European Union), since the move of domicile to another member state is thereby limited.

The European Court argued, that Art. 52 and 58 do not only regulate the case that member states have to allow the establishment of a corporate with the origin of another member state, but next to that a member state cannot limit the move to another member state[17]. Normally, such right of establishment is used in the way that branches or affiliates are opened and registered in another member state[18]. The regulation in Great Britain do not limit such a way of moving but only the case, where the corporate wants to move its domicile to another member state under perpetuation of the legal form as a corporate under English Law[19]. Under reference on the different legal systems on companies in the member states and in particular on the difference between countries, where the legal form of a corporate have to follow its domicile (so called real seat theory) and those, where the legal regime is that of the foundation of a corporate (incorporation theory), the court clarified, that with the European Contracts the national law on companies wasn't touched, but only the freedom of establishment were guaranteed[20]. This would limit national competencies only in the respect, that they would forbid in general the moving to another member state. Since und British Law it is possible to liquidate the corporate and to found a new one in another member state, Art. 52 and 58 are not violated[21], since it is in the competence of every member state to regulate the legal faith of a legal person, only existing because of the national law[22].

To catch the point and to show the differences to other cases below, I would like to point out, that in the Daily Mail Case an authority of the member state, where a corporate exist, do made a decision, interfering in the decision of the corporate to move its domicile.

17 See Point 16 of the reasons.

18 See Point 17.

19 See Point 18.

20 Points 20-23.

21 Point 24.

22 See Point 19.

In German legal publications Daily Mail was taken as the evidence, that the real seat theory is in line with European Law and in particular with Art. 52 and 58[23]. Everything was fine, since if the real seat theory wouldn't but only incorporation theory would be in the frame of European Law, German judges would have to take several legal regimes under account.

2. Centros

After eleven years[24] European Court of Justice had to decide on the Centros case[25]. Here a Danish couple plans to establish a Private Limited Company under British Law, to operate business in Denmark but not to have to get together minimum capital, as it is the case for PLC's in Denmark. Instead of 200.000 Danish Crowns the registered PLC had a capital of 100 British Pound (what was in that time around 1.000 Danish Crowns). The Danish Register office denied the registration of a branch, since the foundation of the LLC in Great Britain was only because of that avoidance of minimum capital but no business was planned there.

The court argued that the decision by the Danish Register Office does harm Art. 52 of the European Treaty, since it denies the registration of a branch of a corporate, established in line with the regulations of a member state[26]. The denial of the registration of a branch would be only legitimate, if it prevents a misuse or fraud[27], but the prevention of minimum capital is not a misuse in that sense[28]. Since the registration would be made, if the corporate do business in Great Britain[29] and under British Law the corporate have to use the abbreviation "PLC" in business relations. By this, it is for everyone clear, that the corporate is not a Danish PLC but one under British Law. Even if the business partner has no knowledge on British PLC and the fact, that they do not need a minimum capital, s/he's warned, that a special legal regime is valid[30].

23 See Ulrich Koch, „Die Entwicklung des Gesellschaftsrecht in den Jahren 1989/90, The development of Company Law in 1989/90", *NJW*, 1992, 404, 412.

24 In the meanwhile there were other decisions on the freedom of establishment, which do not cover the topic handled here, since they handle only violations against directives but not primary European Law. So you can find the Factortame II (C-221/89 from July 25th 1991), Ponente Carni (C-71/91 and C-178/91 from April 4th 1993) Viessmann (C-280/91 from March 18th 1993), Daihatsu (C-97/96 from December 4th 1997) and Lease Plan Luxembourg (C-290/96 from May 7th 1998).

25 C-212/97 from March 9th 1999, available at *http://curia.europa.eu*.

26 See Point 20-22.

27 Point 24-25.

28 Point 27.

29 Point 35.

30 Point 36.

Different as with Daily Mail with Centros not an authority of the country of origin interfere in the corporate decision to move the domicile but the country where the corporate wants to move at. It's even not a case of moving the domicile, since only the registration of a branch was requested. But in the light of the real seat theory it's a question of moving the domicile, since with this theory the real location of the seat has to be taken into account and not only the formal seat, as it is possible within the incorporation theory.

The decision caused a flood of publications[31] since at least German layers fears, that with Centros, the European Court decided, that the real seat theory is not in line with European Law. During that discussion it was clarified, that this question was not subject of Centros, since Denmark is a country, where the incorporation theory is applicable. From that under Danish Law, the question, if a corporate was established in legal way, has to be decided under the legal regime of the foundation of the corporate. This was British Law and with that, the establishment was fine. It would be a different question, if the registration would be requested in member state, where the real seat theory is given, what was not the case[32].

3. Überseering

This time, the German legal community do not have to wait another eleven but only three years, when European Court of Justice had to decide on the Überseering case[33]. In that case a Dutch company sues a German company at a German court. The Dutch Company, the Überseering BV, where the abbrivation is for the Dutch correspondent legal form to limiteds under British Law, had it seat in Germany after all shares were sold to Germans and all activities of the company were only in Germany. The German court had to bring the case to the European Court of Justice since under German Law, the Dutch company would not be accepted as a party in the trial, since its legal regime have to follow the real seat, but no registration was made at the German Company Register. From the point of view of the real seat theory, the Dutch company did simply not exist. After the Dutch company claimed, this would be against Art. 43 and 48 of the EC Treaty[34], the German Court had to do so, since it is within the competence of the European Court of Justice what is in line with European Law and not with the German court.

31 See the list at Palandt, *Kurz-Kommentar zum Bürgerlichen Gesetzbuch, Short Commentary on the Civil Code*, Issue 21th, 2002, cited as Palandt, Heldrich, Att. to Art. 12 German IPR (EGBGB), MN 2.

32 See Peter Kindler, „Niederlassungsfreiheit für Scheinauslandsgesellschaften?, Right of establishment for pseudo-foreign companies?", NJW, 1999, page 1993, page 1997.

33 C-208/00 from November 5th 2002 (since 1997 all decision are available with the Webpage oft he European Court).

34 After Maastricht another numbering took place.

The European Court explicitly decide, that the real seat theory is valid within Europe, since the question isn't harmonized neither with the European contracts nor with additional legal acts on the European level[35]. But the factual results of the application of the real seat theory have to be in line with European Law, in particular with Art. 43 and 48 of the EC Treaty. Even if the application of the real seat theory is in line with European Law, the Court decided, that the Non-Acknowledgement of the corporate as such by a German Authority would neglect the existence of the Company from Dutch Law[36]. In the result, the Court restricted the decision on the case of the ability for being party in civil proceedings[37] and decided that the non-acknowledgement as a party in a civil proceeding would violate Art. 43 and 48 EC Treaty. The German Argumentation, that the non acknowledgement wouldn't be against European Law, since also German companies would be handled in the same way, if they would move their domicile to a foreign country. Additionally the real seat theory would secure creditor interest with respect to different minimum capital regulations, employers rights and fiscal interests[38], was not accepted in the light of the ability being party in a civil trial, where these reasoning do not ask for not acknowledgement of the company[39].

4. Inspire Arts, Cevic and Cartesio

In the following, the opening of the legal forms from other members states was affirmed with the decisions Inspire Arts[40] and Sevic[41]. With Inspire Arts, special regulations on the registration with foreign companies under Dutch Law was forbidden while with Sevic the German regulation, that a merger can be made only with companies under German Law but not with those from a different legal origin, was seen as a violation of Art. 43 and 48 EC Treaty. By that it was somehow surprising, that with Cartesio[42] the Daily Mail decision was affirmed. The case is from special interest for us, since it handle the request of a Hungarian private limited partnership (Kommanditgesellschaft) it goes with a new member state, just harmonized with the acquis communautaire. The European clarified, that, as stated above, it is a different question, if a member state makes regulations with respect

35 See Habersack (FN 9), MN 13b.

36 See Point 81.

37 See Point 82.

38 See Point 85–91.

39 See Point 93.

40 C-167/01 from September 30th 2003.

41 C-411/03 from December 13th 2005.

42 C-210/06 from February 21st 2009.

to legal persons, which are established under its legal regime, if this legal person like to move its domicile to another state, or if a member state restrict the registration of a legal person, established in another member state[43]. All decisions, presented above after Daily Mail handled regulations or legal actions of authorities of the let's called it "receiving" state, while Daily Mail as Cartesio handle with an action by the country of origin.

5. Reactions in Germany

With the Überseering decision the door was opened for a flood of limiteds, established under British Law but operating in other member states. Even if the German legal community try to limit the outcome of the decision to the legal capacity in civil trials, the further reasoning of the European Court were seen as a starting point to offer the legal form of a limited to clients, not at least to prevent the minimum capital. On the peak, 6.000 limiteds were established every year. Since the European Court stated, that only those measures, limiting the freedom of establishment of foreign countries would be in line with Art. 49 and 54 of the Treaty on the Functioning of the European Union, if they do have to legitimated by predominant public interests and no opportunity to react with a measures less interfering. With Inspire Arts relating regulations in Netherlands, which were a direct reaction on Überseering and introduce a special handling of foreign companies were denied as they are violating the freedom of establishment. By this, the European Court opens an opportunity for national regulations but never accept an existing one as legitimated by overwhelming public interest. In particular with respect to the prevention of minimum capital by establishment of pseudo-foreign companies, European Court do not see a legitimation, since by the use of the foreign abbreviation the business community is warned, that the company do not fulfill the conditions of a company, established under national law.

After a real industry was established, offering services to establish limiteds operating outside U.K.. Since British Company Law requires a secretary in Great Britain for being able to receive communication and to represent the with the British authorities, the annual fee for the British registration office and the need for an English of the balance sheet, to be submitted annually to the register office in UK, (legal) running costs of a limited were much higher, while with the German Company with limited liability (GmbH), the establishment costs were higher, since a notary have to be involved and the registration fee were higher than that in UK. Last but not least, British Law do not know the requirement of minimum charter capital, what have to be transferred to the corporate with the registration. Taken this under account, Limiteds were cheaper with the establishment but,

43 Points 120–122.

because of the running costs, more costly after approximately seven years. Despite the fact, that the legal form as a Limited was seen in business practice as a warning signal, like it was stated by the European Court several times, German legislator feared, that the German model will be outdated soon. To prevent this, with the reform of the German Law on Companies with limited liability (GmbHG) a new form was introduced. After a heated discussion, if Germany should remain with the approach, to ask for an obligatory minimum charter capital or if a reduction, in particular for companies in the service sector would be an incentive, to further use German legal forms. At the end, German Parliament enact a reform law on the GmbHG, where the new form of an Entrepreneur Company (Unternehmergesellschaft – UG) was introduced[44]. Unlike the regular Company with limited liability companies, with the Entrepreneur Company no minimum capital is required but the Company has to save at least 25% of their revenues for getting together charter capital up to the time, the charter capital reach the minimum charter capital of a regular Company with limited liability.

Even before, since the disadvantages like high running costs became visible, but now with the back up of a newly introduced form of the Entrepreneur Company, the triumph procession of the Limited was stopped[45], but the developments showed, that next to the legislative activities of the European Union by Directives and Regulations the Court practice do have an enormous impact on the legal practice in Germany[46] and led to legislative changes to react on these practice.

6. Reflections on Serbia

Serbia do follows, as a civil law country, the real seat theory[47] and faces, like Germany did, the impact of the Court practice at least within its efforts to approximate its legal system to the acquis communautaire, where the European Court practice is a part of it. To my knowledge, neither the Law on Companies nor the Law on Registration of Legal Entities do include regulations on the handling of foreign companies. Only with regard to branches, Art. 3 Par. 1 of the Serbian Law on Companies[48] regulates that

44 Gesetz zur Moderniserung des GmbH Rechts und zur Vermeidung von Mißbräuchen (MoMiG), Law on reforming the Law on Companies with limited liabilty and to prevent misuse, OJ I, 2008, 2026 from October 23rd 2008.

45 E.g. Peter Limmer, Von der Limited zur GmbH, From Limited to GmbH, DNotZ 2010, 319.

46 Also other member states like France introduced new forms of limited liability companies but choose the option to reduce the required charter capital.

47 See Art. 16 Par. 1 of the Serbian Law on Companies.

48 Hereby the original version of the Law on Companies is cited. Amendments do not touch regulations, named here.

foreign companies can register a branch, which does not have the status of a legal person. If that is true, Serbia will face the same situation as the old member states of the European Union, in particular with the registration of branches of pseudo-foreign companies with an origin in one member state of the European Union. With the needed consideration, if approximation is needed in that respect, it has to be taken into account, that it would be in Serbian interest to be aware, that within the scope of the Central European Free Trade Agreement it should be prevented, that companies from EU member states should be privileged. From that, considerations could be made to explicitly regulate the registration of companies within foreign origin and of branches of only pseudo-foreign companies in line with the limits, given by the European Court practice. I do hope, that with this paper a contribution to that discussion is made.

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ПРАКСА ЕВРОПСКОГ СУДА ПРАВДЕ О СЛОБОДИ НАСТАЊИВАЊА КОМПАНИЈА У ОКВИРУ ЕВРОПСКЕ УНИЈЕ

У првом делу чланка аутор приказује најзначајније изворе европског компанијског права, који су подељени на примарне и секундарне. Аутор је посебно указао да циљ екстензивне компанијскоправне регулативе у Европској унији није у потпуној унификацији ове области, већ у појединостављивању прекограничних активности.

У другом делу аутор се осврнуо на најзначајније случајеве Европског суда правде, у којима су заузимани далекосежни ставови око граница прокламоване слободе настањивања. Посебно је указано на утицај које су приказане одлуке имале у Немачкој, али и на њихове могуће рефлексије на српско законодавство.

Кључне речи: *европско компанијско право, Европски суд правде, комунитарно право, слобода настањивања.*