ARTICLES

The Legal Framework of Regulatory Competition Based on Company Mobility: EU and US Compared

By Eva-Maria Kieninger[*]

A. Introduction

The phenomenon of regulatory competition, if it exists at all[1], has at least two prerequisites: On the "supply-side" there must be incentives for corporate law-makers to tailor their products according to the needs of those who decide about the place of incorporation (or re-incorporation). On the "demand-side", there must be a real and not only a theoretical possibility to choose the applicable corporate law by choosing the place of (re-)incorporation. Whether such a possibility is a real or theoretical one primarily depends on the costs of such a move compared to its benefits. For the decision about the place of the real seat of a company, "good" or "bad" corporate law is only one factor, very often a minor one among other legal and factual determinants such as corporate and other taxes, labor and environmental law, the accessibility of raw material and product markets or the existence of qualified work force[2]. As long as the choice of a certain corporate law is linked to the choice of the real seat of the corporation, freedom to choose the applicable corporate law only exists on a theoretical level. Corporate law can only be chosen as part of a much larger bundle. If, however, companies are able to opt for a corporate seat that is independent from its real seat (and hence at relatively low costs), the freedom to choose the applicable corporate law becomes a real one and that way the second prerequisite for regulatory competition mentioned above will be fulfilled.

---

[*] Professor of Corporate and Comparative Law, University of Würzburg. Email: kieninger@jura.uni-wuerzburg.de. An earlier version of the paper was presented at the Conference EU Corporate Law Making, Cambridge, Mass., October 29-30, 2004, Section III: Regulatory Competition in the EU.

[1] See the critical article by Marcel Kahan & Ehud Kamar, *The Myth of State Competition in Corporate Law*, 55 STAN. L. REV. 679 (2002).

[2] EVA-MARIA KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT 240 et seq. (2002) for further references.

This article examines the framework of regulatory competition in the EU after the European Court of Justice's (ECJ) landmark decisions in *Centros*[3], *Überseering*[4] and *Inspire Art*[5]. In order to highlight possible shortcomings in the EU, it compares the European status quo with company mobility in the US. It will be shown that although the ECJ's judgments have paved the way for companies to choose their place of incorporation independent from their real seats, re-incorporations, which are crucial for the establishment of corporate law markets, are still severely hampered in the EU.

It is well known, that in the EU the freedom to choose the applicable corporate law through the choice of a corporate seat that is independent from its real seat, is of relatively recent date. It originated in 1999 from the famous *Centros*-judgment of the ECJ[6]. Whereas the general move towards the so-called "incorporation theory" is now practically undisputed, the exact consequences of this judgment and the further development of conflict of laws in the area of company law is still a matter of debate. Part II of this paper will summarize the status quo of the present discussion and try to give some explanations for its development.

---

[3] Case C-212/97, *Centros Ltd. v. Erhvervs- og Selskabsstyrelsen*, decision of 3/9/1999, E.C.R. I-1459 (1999). See Eva Micheler, 52 INTERNATIONAL AND COMPARATIVE LAW QUARTERLY (ICLQ) 521 (2003); Wulf-Henning Roth, *From Centros to Überseering: Free Movement of Companies, Private International Law, and Community Law*, 52 ICLQ 177 (2003). All three decisions have triggered a wealth of literature, primarily in Germany, but also in other Member States. This article only provides selected citations either to comments in English or to articles that focus on questions discussed here in depth.

[4] Case C-208/00, *Überseering B.V. v. Nordic Construction Company Baumanagement GmbH (NCC), decision* of 11/5/2002, referred to the ECJ by the German *Bundesgerichtshof* (BGH), Resolution of 3/30/2000, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 555 (2000) = PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 423 (2000) = ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (ZIP) 967 (2000); final decision of the German *Bundesgerichtshof* (BGH) of 3/13/2003, JURISTENZEITUNG (JZ) 535 (2003) (comment by Horst Eidenmüller) = NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 431 (2003) (comment by Johannes Wertenbruch), NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 618 (2003) = NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 1461 (2003), See Martin Schulz, *(Schein-)Auslandsgesellschaften in Europa - Ein Schein-Problem?,* NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 2705 (2003). See also Mads Andenas, *Free Movement of Companies*, 119 LAW QUARTERLY REVIEW 221 (2003); Kilian Baelz/Teresa Baldwin, *The End of the Real Seat Theory (Sitztheorie): the European Court of Justice Decision in Überseering of 5 November 2002 and its Impact on German and European Company Law*, 3 German Law Journal No. 12 (1 December 2002); Paul Lagarde, 92 REVUE CRITIQUE DE DROIT INTERNATIONAL PRIVÉ 508 (2003); Eva Micheler, 52 ICLQ 521 at 523 et seq. (2003); Wulf-Henning Roth, *From Centros to Überseering: Free Movement of Companies, Private International Law, and Community Law*, 52 ICLQ 177 at 193 et seq. (2003); Ioanna Thoma, *The Überseering ruling: a tale of serendipity*, EUROPEAN REVIEW OF PRIVATE LAW (ERPL) 545 (2003).

[5] Case C-167/01, *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd.*, decision of 9/30/2003. Christian Kersting/Clemens Philipp Schindler, *The ECJ's Inspire Art Decision of 30 September 2003 and its Effects on Practice*, 4 German Law Journal No. 12 (1 December 2003).

[6] See *supra*, n.3.

Some have compared developments in the EU to those in the U.S. Yet what we observe is different. In contrast to the EU, in the U.S. most if not all studies on regulatory competition focus on the *re-incorporation* of companies as opposed to the incorporation of start-ups. There are two main reasons for this: (i) At the start, many companies are incorporated under the laws of their real seat in order to spare the extra costs of franchise tax in Delaware or another state that grants favourable conditions. They are only reincorporated in another state if, due to the success of the business, the benefits of re-incorporation outweigh its costs[7]. (ii) The so-called "event-studies"[8] analyzing moves on the stock markets in relation to a *re-incorporation* decision can by definition only be carried out with *re-incorporation*s. Part C will therefore compare the existence and significance of re-incorporations in the US and the EU.

In the aftermath of *Centros*[9], *Überseering*[10] and *Inspire Art*[11], many authors have expected regulatory competition in company law also to start in the EU. Five years after *Centros,* company law reform is in fact taking place in a number of EU Member States. Are these signs of regulatory competition? Which categories of corporations (large/small, privately/publicly held) are the subject-matter of such a competition (Part D)?.

B. The freedom to choose the place of incorporation for EU-companies - status quo after *Centros*, *Überseering* and *Inspire Art*

---

[7] See Roberta Romano, THE GENIUS OF AMERICAN CORPORATE LAW (1993) p. 6 et seq.; id., *Law as a Product, Some Pieces of the Incorporation Puzzle*, 1 J.L.ECON.ORG. 225, 244 et seq. (1985).

[8] In general, event-studies try to find out whether certain legislative or managerial decisions influence the development of stock prices. In this case, the event is the management's decision to reincorporate in Delaware or another "responsive state". See Roberta Romano, *The Genius of American Corporate Law* (supra note 7, 17 et seq.; Roberta Romano, *Law as a Product, Some Pieces of the Incorporation Puzzle*, 1 J.L.ECON.ORG. 225, 279 et seq. (1985). A survey of further *event-studies* can be found at Roberta Romano, *The State Competition Debate in Corporate Law*, 8 CARDOZO L. REV. 709, 731 et seq. (1987); ID., THE GENIUS OF AMERICAN CORPORATE LAW 17 et seq. (1993). See also recently Lucian Bebchuk, Alma Cohen & Allen Ferrell, *Does the Evidence Favour State Competition in Corporate Law?*, 90 CAL. L. R. 1775, 1790 (2002).

[9] See *supra* n. 3.

[10] See *supra* n. 4.

[11] See *supra* n. 5.

Before 1999, EU Member States were divided on the issue of the relevant connecting factor in company law matters[12]. The United Kingdom, the Netherlands and the Nordic states followed the so-called incorporation theory, according to which the applicable law is determined by the place of incorporation. In practice, this approach enables founders to choose the company law system which they think is best tailored to their needs. It also allows the real seat of a company to be moved to another jurisdiction without triggering a change of the applicable law. Contrastingly, Germany, Austria, France, Belgium, Luxemburg, Portugal and Greece adhered to the so-called real seat theory. Under this approach, the applicable law is defined by the place of the company's central administration. This means that founders have no choice but to establish the company according to the law of the state in which they want to place its central administration. A change of the real seat automatically leads to a change of the applicable law, which often means that the company must be dissolved under the old law and be newly formed under the new one. In Germany, until a decision of the *Bundesgerichtshof* (BGH) of July 1, 2001[13], courts applied the real seat theory in a rigorous manner: A company that had its real seat in Germany but was incorporated under the laws of another state was null and void[14].Italy and Spain remained in between the two groups: In principle both adhered to the incorporation theory but if a company had its real seat in Italy or Spain, both required that the company must also be incorporated under Italian or Spanish law respectively.

I. Centros, Überseering and Inspire Art

In its *Centros*-judgment of March 9, 1999[15], the European Court of Justice (ECJ) decided that a commercial registrar in Denmark could not refuse the registration of a Danish branch of a limited company, incorporated under English law, although the company had its real seat in Denmark. The Danish registrar had argued that Denmark adhered to the incorporation theory only within certain limits. A company

---

[12] For authorities supporting the following text see KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT, supra note 2, 118 et seq. with multiple references.

[13] PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 62 (2003). Comment on the decision by Peter Kindler, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 4 (2003) = DER BETRIEB (DB) 2039 (2002); see also Stefan Leible & Jochen Hoffmann, *Vom "Nullum" zur Personengesellschaft - Die Metarmorphose der Scheinauslandsgesellschaft im deutschen Recht*, DER BETRIEB (DB) 2203 (2002).

[14] One of the consequences was that such a corporation could not bring a law suit, see the case *Überseering*, discussed below, text accompanying note 21.

[15] See *supra*, note 3.

whose sole business activity was carried out in Denmark had to be founded according to Danish law; it had to at least comply with the Danish rules on minimum capital. The ECJ held that *Centros ltd.* made legitimate use of its freedom of establishment when founding a Danish branch. The fact that the whole operation was openly meant to circumvent Danish rules on minimum capital was not regarded as relevant.

After *Centros*, numerous questions remained unanswered: Would the ECJ decide the same way if the subsidiary was founded in a state like Germany that strictly adhered to the real seat theory? Was *Daily Mail*[16] still good law? In that case, decided by the ECJ in 1988, a company founded under English law was prevented by English tax authorities to move its real seat from England to the Netherlands. Although the concerned neither corporate nor private international law, because under both English and Dutch conflicts rules (incorporation theory) it was possible to move the real seat of a company, the ECJ said (obiter) that the freedom of establishment had no impact on the connecting factor in company law matters. In the absence of an international treaty or an EC-harmonisation measure the matter was - for the time being (!) - left to the autonomous decision of the Member States. *Daily Mail*, was not mentioned by the ECJ's ruling in *Centros*. A vigourous debate about the impact of *Centros* on the real seat theory began.[17] In Germany, academic opinion was divided[18]. The courts nearly unanimously tried to save the real seat theory by

---

[16] Case 81/87, *The Queen v. H.M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust PLC*, decision of 9/27/1988, E.C.R. 5483 (1988).

[17] For a comprehensive list of literature on *Centros* see Thomas Bachner & Martin Winner, *Das österreichische internationale Gesellschaftsrecht nach Centros*, DER GESELLSCHAFTER (GESRZ) 73 at 76, note 31 (2000).

[18] As to the transition to the theory of incorporation see Peter Behrens, *Das Internationale Gesellschaftsrecht nach dem Centros-Urteil des EuGH*, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 323 (1999); Volker Geyrhalter, *Niederlassungsfreiheit contra Sitztheorie - Good Bye "Daily Mail"?*, EUROPÄISCHES WIRTSCHAFTS- UND STEUERRECHT (EWS) 201, 203 (1999); José Christian Cascante, *Anmerkungen zu Centros*, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 450, 451 (1999); Robert Freitag, *Der Wettbewerb der Rechtsordnungen im Internationalen Gesellschaftsrecht*, EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (EUZW) 267, 269 (1999); Eva-Maria Kieninger, *Niederlassungsfreiheit als Rechtswahlfreiheit*, ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT (ZGR) 724, 737 et seq. (1999); Stefan Leible, *Anmerkung zu Centros*, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 300, 301 (1999); Wienand Meilicke, DER BETRIEB (DB) 627 (1999); Günter Roth, *Gründungstheorie: Ist der Damm gebrochen?*, ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (ZIP) 861, 867 (1999); Erik Werlauff, *Ausländische Gesellschaft für inländische Aktivität*, ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (ZIP) 867, 875 (1999). For a different view (continuity of the theory of the real seat) see among others Werner Ebke, *Das Schicksal der Sitztheorie nach dem Centros-Urteil des EuGH*, JURISTENZEITUNG (JZ) 656 (1999); Peter Kindler, *Niederlassungsfreiheit für Scheinauslandsgesellschaften*, Neue Juristische Wochenschrift (NJW) 1993, 1996 et seq. (1999). The fact that the Dutch *Wet op de formeel buitenlandse vennootschappen (WFBV)* of 12/17/1997 (*Staatsblad van het Koninkrijk der Nederlanden* 1997, Nr. 697) would be inconsitent with the freedom of establishment was foreseen by: Eva-Maria Kieninger, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT

distinguishing *Centros* and by violating their duty to refer the questions to the ECJ under Art. 234 TEC[19]. The Austrian Supreme Court, however, only a few months after *Centros*, held that in a comparable case involving an Austrian branch of a pseudo foreign corporation founded under English law, Austrian law could no longer negate the legal existence of the corporation. The court explicitly applied the freedom of establishment as limiting the real seat theory[20].

As mentioned earlier, until July 1, 2001 the cases in Germany held that a company that had its real seat in Germany but was not founded in one of the forms that German company law offered, was null and void. In the *Überseering* case[21], this led to strange consequences: *Überseering BV* was a company founded under Dutch law. On account of a transfer of all its shares to two Germans, its real seat had been transferred to Germany,. There, *Überseering* tried to bring an action for payment of a contractual claim. Interestingly, because of the circumstances of the case, German courts were the only possible forum for that claim. However, the BGH denied *Überseering*'s legal capacity to bring a claim in a German court. Because it was a pseudo-foreign corporation, it was void and hence lacked legal personality. It was not the BGH's company law senate[22] but another branch, usually dealing with construction cases, which referred the case to the ECJ. The outcome was no surprise: Denying

---

141 (2002); Harm-Jan de Kluiver, *De wet formeel buitenlandse vennootschappen op de tocht?,* WEEKBLAD VOOR PRIVAATRECHT, NOTARIAAT EN REGISTRATIE (WPNR) 527 (1999); Hans de Wulf, *Centros: vrijheid van vestiging zonder* race to the bottom, ONDERNEMINGSRECHT 318, 320 (1999); Levinus Timmerman, *Das niederländische Gesellschaftsrecht im Umbruch*, FESTSCHRIFT FÜR MARCUS LUTTER 173, 185 (2000).

[19] See *Oberlandesgericht* (OLG) (court of appeals) Düsseldorf, decision of 3/26/2001, ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (ZIP) 790 (2001) = NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 506 (2001), comment by Eva-Maria Kieninger, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 610 (2001); *Oberlandesgericht* (OLG) (court of appeals) Hamm, decision of 2/1/2001, ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (ZIP) 791 (2001) = NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 562 (2001), comment by Günter Chr. Schwarz, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 613 (2001).

[20] *Oberster Gerichtshof* (OGH) (Austrian Supreme Court), decision of 7/15/1999, ÖSTERREICHISCHES RECHT DER WIRTSCHAFT (RDW) 719 (1999) (comment by Christian Nowotny) = DER GESELLSCHAFTER (GESRZ) 248 (1999) (comment by Thomas Bachner) = NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 36 (2000) (comment by Eva-Maria Kieninger) = JURISTENZEITUNG (JZ) 199 (2000) (comment by Gerald Mäsch); see also Peter Behrens, *Reaktionen mitgliedstaatlicher Gerichte auf das Centros-Urteil des EuGH*, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 384, 386 et seq. (2000); Barbara Höfling, *Die Sitztheorie, Centros und der österreichische OGH*, EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (EUZW) 145 (2000).

[21] See *supra*, n. 4.

[22] Unlike the Highest Courts of other jurisdictions, the German Federal Court of Justice (*Bundesgerichts - hof*, BGH) consists of 24 chambers (so-called senates) of whom 12 are dealing with civil law cases, five with criminal cases and seven with special matters, such as competition law or intellectual property rights.

Überseering's legal capacity to bring an action for a payment which without doubt was owed to the company, in a situation where the only possible forum was a German court, amounted to a deprivation. To state that the real seat theory worked for the benefit of a company's creditors by depriving the company of its possibility to collect its claims was as unconvincing as Germany's argument in *Cassis de Dijon* had been, where it had been said that a certain minimum alcohol content improved people's health. The company law senate of the BGH tried to influence the ECJ's attitude against the real seat theory in the very last minute by deciding, between the request for a preliminary ruling and the ECJ's decision in *Überseering*, that in another case similar to *Überseering*, a pseudo-foreign-corporation could be treated as a partnership and hence at least be able to bring a court action[23].This approach, however, was not brought to the attention of the ECJ. The Court decided that due to Art. 43, 48 TEC German law must recognize a foreign company *as it was founded* provided that it was lawfully incorporated according to the laws of another EU Member State.[24]

From this decision on, in cases involving EU-Member States, German courts have unanimously abandoned the real seat theory and have applied the law of the place where the foreign company is incorporated[25]. Some writers' attempts to limit the impact of the ECJ's decision to the recognition of legal personality and to deny its influence on questions of minimum capital and personal liability of directors and shareholders[26] proved ultimately fruitless . Remaining doubts in this respect have been removed by the third decision of the ECJ, *Inspire Art*[27]. *Inspire Art* again con-

---

[23] BGH, 1.7.2002, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 62 (2003) withcomment by Peter Kindlerat p. 4 = DER BETRIEB (DB) 2039 (2002); see also Stefan Leible & Jochen Hoffmann, *Vom "Nullum" zur Personengesellschaft - Die Metarmorphose der Scheinauslandsgesellschaft im deutschen Recht*, DER BETRIEB (DB) 2203 (2002).

[24] See supra, note 4, para 80.

[25] In addition to the decision of the *Bundesgerichtshof* (BGH) of 3/13/2003 (see *supra* note 21) see also *Bayerisches Oberstes Landesgericht* (BayObLG) (court of appeals for selected matters in Bavaria), decision of 12/19/2002, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 290 (2003), discussed by Stefan Leible & Jochen Hoffmann, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 259 (2003); *Oberlandesgericht* (OLG) (court of appeals) Celle, decision of 12/10/2002, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS IPRax 245 (2003); *Oberlandesgericht* (OLG) (court of appeals) Zweibrücken, decision of 3/26/2003, BETRIEBSBERATER (BB) 864 (2003); *Kammergericht* (KG) (Berlin court of appeals), decision of 11/18/2003, BETRIEBSBERATER (BB) 2644 (2003); for further reference of unpublished case law of trial courts see Stefan Leible & Jochen Hoffmann, *"Überseering" und das deutsche Gesellschaftskollisionsrecht*, ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (ZIP) 925, 927 (2003).

[26] See in particular Holger Altmeppen, *Schutz vor "europäischen Kapitalgesellschaften"*, NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 97 (2004).

[27] See *supra* n. 5.

cerned an English limited company whose sole activities were carried out in the Netherlands. Dutch law followed the incorporation theory, but withcertain limits. Comparable to the pseudo-foreign corporation statutes of New York or California[28], corporations doing business in the Netherlands must comply with certain compulsory rules, e.g. rules on minimum capital[29]. If they do not comply, the directors are personally liable for the company's debts. The ECJ held that the application of these rules to companies incorporated under the laws of another EU-Member State violated the freedom of establishment[30]. Again, the Court saw no abuse in the fact that incorporation under English law rather than under Dutch law had been sought solely in order to circumvent the latter's stricter rules on minimum capital.[31]

II. Answers and new questions

Today, it is safe to say that at the time of incorporation, the members of the company or the directors who act for them, are free to choose any of the now 25 EU-Member States as the place of incorporation and hence their law as the applicable one without running the risk that the company might be considered null and void. Discussion has moved away from the debate between real seat theory and incorporation theory to more subtle distinctions.

1. "Move in" and "move out" cases

As stated earlier In 1988, before *Centros*, *Überseering* and *Inspire Art,* the ECJ had to decide the already mentioned *Daily Mail* case[32] which involved the attempt to move a company's real seat away from its state of incorporation.The Court found no violation of EC-law in the fact that the state of incorporation did not allow such a move. *Daily Mail* was not mentioned by the ECJ in *Centros* or *Überseering*. In *Inspire Art*, the ECJ distinguished *Daily Mail* without, however, overruling the decision. In

---

[28] See N.Y. Bus. Corp. Law § 1320 (2003) and Cal. Corp. Code § 2115 (2003); See further *Kersting*, Corporate Choice of Law, A Comparison of American and European Systems and a Proposal for a European Directive, 28 BROOKLYN J. INT. L. 1 at 26 et seq. (2002).

[29] *Wet op de formeel buitenlandse vennootschappen (WFBV)* of 12/17/1997, Staatsblad van het Koninkrijk der Nederlanden 1997, No. 697.

[30] In the same direction before *Inspire Art*, Harm-Jan de Kluiver, *De wet formeel buitenlandse vennootschappen op de tocht?,* WEEKBLAD VOOR PRIVAATRECHT, NOTARIAAT EN REGISTRATIE (WPNR) 527 (1999); Hans de Wulf, *Centros: vrijheid van vestiging zonder* race to the bottom, ONDERNEMINGSRECHT 318, 320 (1999); Levinus Timmerman, *Das niederländische Gesellschaftsrecht im Umbruch*, in: FESTSCHRIFT FÜR MARCUS LUTTER 173, 185 (2000).

[31] See *supra*, note 5, para. 137.

[32] See *supra* note 16.

Inspire Art, the Court characterized *Daily Mail* as a case concerning the impact of the laws of the state of incorporation on the conditions of the company's continuing existence. Contrastingly, the Court regarded *Centros*, *Überseering* and *Inspire Art* as cases which concerned the impact of the laws at the company's new home. The state to which the company had been moved could not, without violating Art. 43, 48 TEC, refuse to recognize the company's existence or place its continuation under restrictive conditions such as the unlimited liability of the shareholders.

This distinction between "move in" and "move out" cases leads to the result that, e.g., German law must accept pseudo-foreign corporations moving to Germany, but is still free to deny companies founded under German law the power to move elsewhere, even if such a move concerns both the real and the statutory seat. In other words: Other Member states are obliged to welcome the German company, thus to enable it to make use of its freedom of establishment, but Germany as the state of origin can still prevent the company from moving by regarding the shareholders' decision to move it as a decision to dissolve it. It is needless to say, that many commentators regard this state of affairs as unsatisfactory and urge a revision of autonomous national conflicts law, at least until the ECJ modifies its position[33].

2. The scope of the theory of incorporation

a) Protection of creditors - minimum capital and piercing the corporate veil

Another point of concern is the determination of the scope of the new approach[34]. To what extent is a company founded under the laws of Member State A bound by

---

[33] Walter Bayer, *Die EuGH-Entscheidung "Inspire Art" und die deutsche GmbH im Wettbewerb der europäischen Rechtsordnungen*, BETRIEBSBERATER (BB) 2357, 2363 (2003); Peter Behrens, *Gemeinschaftsrechtliche Grenzen der Anwendung inländischen Gesellschaftsrechts nach* Inspire Art, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 20, 26 (2004); Werner Ebke, *Überseering: "Die wahre Liberalität ist Anerkennung"*, JURISTENZEITUNG (JZ) 927, 932 (2003); Eva-Maria Kieninger, *Internationales Gesellschaftsrecht nach „Centros", „Überseering" und „Inspire Art": Antworten, Zweifel und offene Fragen*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEUP) 685, 694 et seq. (2004).

[34] This is the new focus of the discussion, see Walter Bayer, *Die EuGH-Entscheidung "Inspire Art" und die deutsche GmbH im Wettbewerb der europäischen Rechtsordnungen,* BETRIEBSBERATER (BB) 2357 (2003); Peter Behrens, *Gemeinschaftsrechtliche Grenzen der Anwendung inländischen Gesellschaftsrechts nach* Inspire Art, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 20 (2004); id., *Das Internationale Gesellschaftsrecht nach dem Überseering-Urteil des EuGH und den Schlussanträgen zu Inspire Art*, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 193 (2003); Tim Drygala, *Stand und Entwicklung des europäischen Gesellschaftsrechts*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEUP) 337 (2004); Eva-Maria Kieninger, *Internationales Gesellschaftsrecht nach „Centros", „Überseering" und „Inspire Art": Antworten, Zweifel und offene Fragen*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEUP) 685, 696 et seq. (2004); Horst Eidenmüller & Gebhard Rehm, *Niederlassungsfreiheit versus Schutz des inländischen Rechtsverkehrs: Konturen des Europäischen Internationalen Gesellschaftsrechts,* ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT (ZGR) 159 (2004); Otto Sandrock, *Was ist erreicht? Was bleibt zu tun? Eine*

the rules of Member State B, where it has its real seat? The ECJ has left two remaining grounds for applying the law of the real seat.

One is the well-known *Cassis* formula of "mandatory requirements of public interest".[35] In *Centros*[36] and *Inspire Art*[37], the Court did, as a matter of principle, acknowledge that the protection of creditors may be a legitimate mandatory requirement. But the decisions themselves left very little room for most national protective measures, as the Danish and Dutch minimum capital provisions in question did not pass the further tests of necessity and proportionality. The Court correctly held that creditors could inform themselves about the fact that they dealt with a foreign company which might not be subject to domestic rules. In *Centros*, the Court added - even more persuasively - that the creditors of the Danish branch would have been equally endangered by the activities in Denmark of an undercapitalized English company if that company was also carrying on activities in England, a case in which the Danish registrar would not have hesitated to register the branch. It seems therefore safe to conclude that minimum capital requirements and similar provisions at the real seat can no longer be imposed on companies founded in other Member States. Of course, to an American corporate lawyer this debate on minimum capital may seem completely unnecessary and outdated. Legislation in the US long ago abandoned the whole concept of minimum capital because it often failed to meet its goals.[38] Other methods like self help of creditors (covenants, security rights) or piercing the corporate veil substitute capital requirements. However, in the mind of a German corporate lawyer, the idea that a company must have a minimal fund as a guarantee of payment and as a compensation for its limited liability is so firmly embedded that it seems hard for him to perceive a system which

---

kollisions- und materiellrechtliche Bilanz, in: OTTO SANDROCK & CHRISTOPH WETZLER (eds.), DEUTSCHES GESELLSCHAFTSRECHT IM WETTBEWERB DER RECHTSORDNUNGEN 33 (2004); Otto Sandrock, *Die Schrumpfung der Überlagerungstheorie,* 102 ZEITSCHRIFT FÜR VERGLEICHENDE RECHTSWISSENSCHAFT (ZVGLRWISS) 447 (2003); Gerald Spindler & Olaf Berner, *Der Gläubigerschutz im Gesellschaftsrecht nach Inspire Art*, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 7 (2004); CHRISTOPH WETZLER, *Rechtspolitische Herausforderungen,* in: OTTO SANDROCK & CHRISTOPH WETZLER (eds.), DEUTSCHES GESELLSCHAFTSRECHT IM WETTBEWERB DER RECHTSORDNUNGEN 129, 161 et seq. (2004).

[35] Case C-120/78, *Rewe-Zentral-AG/Bundesmonopolverwaltung für Branntwein*, decision of 20/2/1979, E.C.R. 649 (1979) para. 8.

[36] See *supra*, note 3, para. 34 et seq.

[37] See supra note 5, para 133 et seq.

[38] William Carney, *The Political Economy of Competition for Corporate Charters*, 26 J.LEGAL STUD. 303 at 323 et seq. (1997); Alfred Conard, *The European Alternative to Uniformity in Corporation Laws*, 89 MICH.L.REV. 2150 at 2172 et seq. (1991); FRIEDRICH KÜBLER, AKTIE, UNTERNEHMENSFINANZIERUNG UND KAPITALMARKT (1989) 22 et seq.

operates without it, although one must admit, that even German company lawyers have come to admit, that 25.000.- € for a private limited company and 50.000.- € for a public company is not more than a "*Seriositätsindiz*" (indication of seriousness)[39].

This leaves the second possible basis for inroads into the theory of incorporation. This is the notion of "abuse of the freedom of establishment". In *Centros*[40] and *Inspire Art*[41], the ECJ emphasized that Member States remain free to combat misuse of the freedom of establishment in individual cases. According to the ECJ, the mere fact of setting up a foreign company in circumvention of domestic capital requirements alone does not constitute an abuse of the freedom of establishment. So, what else can be considered an abuse? Many German authors equate abuse of the freedom of establishment with the abuse of limited liability[42], e.g. in cases of a so-called "*existenzvernichtender Eingriff*"[43]. These are cases where systematic violations of the duty to separate the company's patrimony from the main shareholder's patrimony lead to personal liability of the latter. Without questioning the justification of personal liability in such instances, doubts remain whether it is compatible with the ECJ's jurisprudence to draw the foundation of liability from the law at the real seat of the company, while overriding or neglecting the applicability of the law at the statutory seat. In other words, it is doubtful whether it is appropriate to equate abuse of the freedom of establishment with abuse of limited liability [44]. The notion of abuse

---

[39] See Marcus Lutter, *A Mini-Directive on Capital*, in: HARM-JAN DE KLUIVER & WALTER VAN GERVEN (eds.), THE EUROPEAN PRIVATE COMPANY? 201, 202 et seq. (1995).

[40] *Supra* note 3, para. 24 et seq.

[41] *Supra* note 5, para 136 et seq.

[42] Horst Eidenmüller, *Anmerkungen zu „Überseering"*, JURISTENZEITUNG (JZ) 526, 529 (2003); Peter Kindler, *„Inspire Art" – Aus Luxemburg nix Neues zum internationalen Gesellschaftsrecht*, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 1086, 1089 (2003); Tim Drygala, *Stand und Entwicklung des europäischen Gesellschaftsrechts*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEuP) 337, 347 (2004,); NORBERT HORN, *Deutsches und europäisches Gesellschaftsrecht und die EuGH-Rechtsprechung zur Niederlassungsfreiheit - Inspire Art*, NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 893, 899 (2004). See also *Amtsgericht* (AG) (court of first instance) Hamburg, decision of 5/14/2003, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 732 (2003) = PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 534 (2003).

[43] An "*existenzvernichtender Eingriff*" is an abuse of the company's patrimony by a dominant shareholder (often the mother company) which leads to a destruction of the company's financial basis, see the leading cases *Bremer Vulkan, Bundesgerichtshof* (BGH) decision of 9/17/2001, *Entscheidungen des Bundesgerichtshofs in Zivilsachen* (BGHZ) 149, at 10, and *Bundesgerichtshof* (BGH) decision of 6/24/2002, JURISTENZEITUNG (JZ) 1047 (2002) (comment by Peter Ulmer). See also Peer Zumbansen, *Liability within Corporate Groups ("Bremer Vulkan"): Federal Court of Justice Attempts the Overhaul*, 3 GERMAN LAW JOURNAL No. 1 (1 January 2002).

[44] See also Eva-Maria Kieninger, *Internationales Gesellschaftsrecht nach „Centros", „Überseering" und „Inspire Art": Antworten, Zweifel und offene Fragen*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEuP) 685, 699 (2004).

of limited liability is inevitably linked to a specific idea of *legitimate* use of limited liability. In absence of European legislation such definitions must necessarily stem from domestic law. In Germany, for example, it is a firmly embedded idea, that limited liability (and legal personality) requires a certain minimum capital. Allowing courts to fall back on the law of the real seat to enforce domestic rules on abuse of legal personality, will inevitably lead back to the application of domestic rules on minimum capital and creditor protection. Therefore, the ECJ cannot be expected to leave the application of such rules of the law at the real seat untouched. At least, the Court is likely to insist on a primary application of the law of incorporation. In turn, this leads to a disregard of the law at the real seat whenever a rule can be found in the law of incorporation which is able to protect the interests in question, even if it does so in a different manner or to a somewhat lesser degree.

b) Application of the law of the real seat under tort or insolvency law

As we have just seen the debate has primarily been evolving around the question to which degree – if at all – the law at the real seat of the company can come into play in cases of an alleged or presumed 'improper' use of limited liability. Clearly, this debate reflects much of what European company law harmonization has been concerned with from its beginning – national particularities and traditions, legal and economic differences. Attempts made, for example, to mitigate the application of the ECJ's rulings by recharacterising issues of law[45], must be seen in this light. And at the same time, there is much merit in a sophisticated application of law to cases that play on the disputed borders between corporate and insolvency law, where the need to protect investors and creditors is assessed from different angles at the same time. In this respect, it is indeed a challenge to draw the lines between corporate, insolvency or tort law when the task is to characterise a company' director's duty to initiate insolvency proceedings at the moment in which the company turns insolvent and to refrain from (fraudulently) carrying on business at the expense of creditors. Such characterisation would lead to the applicability of the law at the real seat, as both the *lex loci delicti* under art. 3 (1) and (2) of the forthcoming Rome-II regulation[46] and the *lex fori concursus* applicable for the main insolvency proceedings under Art. 3 (1) and 4 (1) of the EC Insolvency Regulation[47].

---

[45] See Peter Kindler, *„Inspire Art" – Aus Luxemburg nichts Neues zum internationalen Gesellschaftsrecht*, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 1086 (2003).

[46] COM (2003) 427 final, http://europa.eu.int/eur-lex/en/com/pdf/2003/com2003_0427en01.pdf. Presently a similar rule is in force in most if not all Member States' autonomous conflicts laws)

[47] (Regulation 1346/2000 of May 29, 2000, O.J. 2000 No. L 160 /1 et seq, http://europa.eu.int/eur-lex/pri/en/oj/dat/2000/l_160/l_16020000630en00010018.pdf

However, other authors, including the author of this paper, do not consider such recharacterisation to be a possible way to escape the ECJ's verdict[48] It goes without saying that companies are bound by the general legal rules of the place where they engage in market activities. This includes duties of managers and shareholders under general tort law. Yet, when it comes to duties that are specifically designed to protect interests of members of the corporation or creditors who deal with the company or when it comes to rules which lead to disregarding the limited liability of the corporation, the realm of general tort law is left behind, and company law comes into play. Such issues should be left to the applicable company law as defined by the incorporation theory. Moreover, even if it was correct from a purely private international law point of view to qualify such rules on directors' duties as part of tort law and hence to apply the *lex loci delicti*, this would presumably have no impact on the decisions of the ECJ. As the Court has demonstrated in its *Ingmar* decision[49], it does not pay attention to the subtle distinctions of conflicts theory but solely regards the influence which a certain decision will have on the Common Market.

In sum, the discussion to date has focussed on the scope of the applicability of the law of incorporation. Attempts, however, to override the incorporation law and to apply the law of the real seat can only be successful in cases of a gap in the law of incorporation. In those cases, mandatory requirements of general interest would otherwise remain unprotected. The absence of minimum capital requirements, however, cannot be considered to be such a gap as long as a European debate continues about the different approaches existing in Member States' company laws with regard to creditor protection. This is certainly one important lesson that can be learned from the discussion in Germany with regard to the alleged introduction of

---

[48] Peter Behrens, *Gemeinschaftsrechtliche Grenzen der Anwendung inländischen Gesellschaftsrechts auf Auslandsgesellschaften nach Inspire Art. Anmerkung zu EuGH, U. v. 30.09.2003 - Rs. C-167/01 - (Kamer van Koophandel en Fabrieken voor Amsterdam / Inspire Art Ltd.),* PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 20, 26 (2004), id., *Das Internationale Gesellschaftsrecht nach dem Überseering-Urteil des EuGH und den Schlussanträgen zu Inspire Art*, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 193, 206 (2003); Eva-Maria Kieninger, *Internationales Gesellschaftsrecht nach „Centros", „Überseering" und „Inspire Art": Antworten, Zweifel und offene Fragen*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEUP) 685, 697 (2004); Gerald Spindler & Olaf Berner, *Der Gläubigerschutz im Gesellschaftsrecht nach Inspire Art*, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 7, 9 et seq. (2004). Unclear Walter Bayer, *Die EuGH-Entscheidung "Inspire Art" und die deutsche GmbH im Wettbewerb der europäischen Rechtsordnungen*, BETRIEBSBERATER (BB) 2357 (2003), who on the one hand at p. 2364 et seq. seems to be of the opinion that the liability of the members of a company can not be measured against the freedom of establishment after the requalification as an issue of torts, but on the other side at the end of his article at p. 2365 can already see the "sword of Damokles of a deviating evaluation by the ECJ" above his approach.

[49] Case C-381/98, *Ingmar GB Ltd. v. Eaton Leonard Technologies Inc.*, decision of 11/9/2000, E.C.R. I-9305 (2000).

limited liabilities companies from Great Britain and elsewhere onto the German market.[50]

3. Non-EU Member States

Another central question is the applicability of the theory of incorporation to companies incorporated under the laws of non-EU-Member States. As to US-corporations, Germany is bound to apply the law at the statutory seat by virtue of a bilateral agreement of 1954[51], a fact that seems to have been overlooked in the whole discussion about the threat of a Delaware-effect in the EU. The best chances to become a "European Delaware" (but perhaps with lesser impact on the corporate law of publicly held companies[52]) may be accorded to Liechtenstein, a small principality near Austria and Switzerland. Liechtenstein is a member of the European Economic Area (EEA); its companies have a right to the freedom of establishment. The *Centros* doctrine is therefore fully applicable to companies founded under Liechtenstein law. This has recently been acknowledged by German courts[53]. Liechtenstein itself follows the theory of incorporation and is very active (and successful) in attracting companies through a largely deregulated and permissive company law. As a member of the EEA, it has to comply with the EU-company law directives. But since those are only applicable to certain forms of corporations, the most

---

[50] See, e.g., Alexander Hirsch & Richard Britain, *Artfully Inspired - Werden deutsche Gesellschaften englisch?,* NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 1100 (2003); Walter Bayer, *Die EuGH-Entscheidung "Inspire Art" und die deutsche GmbH im Wettbewerb der europäischen Rechtsordnungen,* BETRIEBSBERATER (BB) 2357 (2003); Peter Behrens, *Gemeinschaftsrechtliche Grenzen der Anwendung inländischen Gesellschaftsrechts nach* Inspire Art, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 20 (2004); Eva-Maria Kieninger, *Internationales Gesellschaftsrecht nach „Centros", „Überseering" und „Inspire Art": Antworten, Zweifel und offene Fragen*, ZEITSCHRIFT FÜR EUROPÄISCHES PRIVATRECHT (ZEUP) 685 (2004); Horst Eidenmüller & Gebhard Rehm, *Niederlassungsfreiheit versus Schutz des inländischen Rechtsverkehrs: Konturen des Europäischen Internationalen Gesellschaftsrechts,* ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT (ZGR) 159 (2004); Gerald Spindler & Olaf Berner, *Der Gläubigerschutz im Gesellschaftsrecht nach Inspire Art*, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 7 (2004).

[51] See *Bundesgerichtshof* (BGH), decision of 1/29/2003, BETRIEBSBERATER (BB) 810 (2003); BGH, decision of 5/7/2004, BB 1868 (2004); BGH, decision of 13/10/2004, ZEITSCHRIFT FÜR INSOLVENZPRAXIS (ZIP) 2230 (2004). See also *Jens Damann*, Amerikanische Gesellschaften mit Sitz in Deutschland, 68 RABELSZ 607 (2004).

[52] In the US, Delaware is mostly attracting large, publicly held companies listed on the stock exchange. Contrastingly, Liechtenstein is mostly sought as a corporate home by privately held companies. This is partly due to the fact that European company law harmonisation extends to public companies incorporated in Lichtenstein.

[53] *Oberlandesgericht* (OLG) (court of appeals) Frankfurt a.M., decision of 5/28/2003, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 56 (2004); SeeCarl Baudenbacher & Dirk Buschle, *Niederlassungsfreiheit für EWR-Gesellschaften nach* Überseering, PRAXIS DES INTERNATIONALEN PRIVAT- UND VERFAHRENSRECHTS (IPRAX) 26 (2004).

successful kinds of Liechtenstein corporate bodies (*Anstalten*, *Stiftungen*) are not affected by European legislation. Of course, this is no coincidence. Liechtenstein obtains a large part of its tax income from a company tax that is comparable to the franchise tax in the US[54]. Having only an extremely small territory with negligible industrial potential, financial services are the main foundation of Liechtenstein's wealth. Considering the fact that the EU-Member States are already obliged to recognize corporations registered in Delaware or Liechtenstein, it seems difficult to deny application of the theory of incorporation to companies formed in other non-EU-Member states. Neither the applicability of EU company law nor the permissive character of domestic law seem to be valid criteria for such a distinction.

4. A brief comparison with US law

To conclude the previous discussion, companies today enjoy the freedom to incorporate in any Member State of the EU and choose their real seat and main field of activity in another Member State, be it directly (*Inspire Art*) or through a branch (*Centros*). A company may also later in its life move its real seat to another Member State. The state of arrival is obliged to continue to apply the law of incorporation (*Überseering*). However, the state of departure is probably still free to undermine the move through a compulsory dissolution (*Daily Mail*). Attempts to avoid these rules by applying the law of the real seat of the company, based upon the notion of mandatory requirements in the public interest or abuse of the freedom of establishment are probably fruitless endeavors.

In the United States, the mobility of companies is both smaller and wider. It is smaller because the theory of incorporation is applied in a more limited way. According to the doctrine of pseudo-foreign corporations[55] the state of the company's real seat may apply certain mandatory rules of its own corporation law if the company conducts its business either exclusively or mainly within that state. Such so-called "outreach statutes" exist primarily in New York and California but also in other states.[56] There is some debate whether outreach statutes may be unconstitutional, as some have accorded constitutional character to the internal affairs rule, but so far, there is no decisive case law[57]. In the EU, on the other hand, *Inspire Art* has clearly shown that pseudo-foreign corporation statutes are contrary to EC-law.

---

[54] See the data provided by KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT (supra n. 2). 186 et seq.

[55] Elvin R. Latty, *Pseudo-Foreign Corporations*, 65 YALE L.J. 137 (1955).

[56] See above, note 28.

[57] See the cases and case-notes cited in EVA-MARIA KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT 110 et seq. (2002).

But at the same time company mobility is wider in the US. So far, it is not possible in the EU to move the corporate seat of an existing company without its real seat; even the freedom to move the corporate seat together with the real seat is still - in the absence of ECJ case law - a matter of debate. In other words, there is no freedom of re-incorporation in the EU, whereas re-incorporation on the US is not only clearly possible but also the predominant form of company mobility which drives regulatory competition (if the latter exists at all). Part C. will examine re-incorporation more closely. But first, let us explore some tentative explanations for the current status of the law in the EU.

III. Some tentative explanations for the development of European conflicts law in company law matters

When regarding the development over the last decades, a number of questions arise. They do not only concern the legislators on the national (1) and European level (2) but also the ECJ (3).

1. National law

Why did German legislators, courts and the predominant academic opinion adhere to the real seat theory for decades despite its disadvantages? Why did *Centros* meet with so much opposition especially in Germany, so that two more decisions of the ECJ were needed before the incorporation theory was firmly established in practice?

The real seat theory was always defended as a "protective theory". Protection was thought to be needed for domestic creditors (contractual and non-contractual, i.e. tort creditors), minority shareholders and - above all - codetermination. However, the real seat theory was not approved of because of its consequences on companies that were in fact established under a foreign law (see e.g. the detrimental consequences of the real seat theory for creditors of the company in the *Überseering*-case) but for its chilling effect. The threat that a pseudo-foreign company would not be recognized as a legal entity at all, or at best be regarded as a partnership with unlimited liability[58], was thought to effectively deter anyone from incorporating under a foreign law if they planned to place their central administration and to conduct their main business activities in Germany. The little case law on pseudo-

[58] See supra text accompanying note 23.

foreign corporations that existed before *Centros*[59] seems to prove that the approach was effective.

Several German corporate law scholars – among them *Sandrock*[60], *Behrens*[61], *Drobnig*[62] and *Knobbe-Keuk*[63] - attacked the real seat theory with well-founded arguments but without effect on the German legislator or the courts[64], although in general, academics in Germany have quite a large influence on legislative and court decisions, especially in a field like private international law which is thought to be highly theoretical, impenetrable and best left to specialists[65]. The perseverance of German courts and the inactivity of the legislator was supported by the ECJ's *obiter dictum* in *Daily Mail*. Since then, responsibility was deemed to have shifted to the European Court. Also, three highly influential commentators, *Großfeld*[66], *Ebenroth*[67] and *Kindler*[68] remained hostile towards the incorporation theory. *Kindler* in particu-

---

[59] See *supra* note 3.

[60] Otto Sandrock, *Ein amerikanisches Lehrstück für das Kollisionsrecht der Kapitalgesellschaften,* 42 RABELS ZEITSCHRIFT FÜR AUSLÄNDISCHES UND INTERNATIONALES PRIVATRECHT (RABELSZ) 227 (1978).

[61] Peter Behrens, *Die Umstrukturierung von Unternehmen durch Sitzverlegung oder Fusion über die Grenze im Licht der Niederlassungsfreiheit im Europäischen Binnenmarkt (Art. 52 und 58 EWGV),* ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT (ZGR) 1 (1994).

[62] Ulrich Drobnig, *Gemeinschaftsrecht und internationales Gesellschaftsrecht - „Daily Mail" und die Folgen,* in: CHRISTIAN VON BAR (ed.), EUROPÄISCHES GEMEINSCHAFTSRECHT UND INTERNATIONALES PRIVATRECHT, 185 (1991).

[63] Brigitte Knobbe-Keuk, *Umzug von Gesellschaften in Europa,* 154 ZEITSCHRIFT FÜR DAS GESAMTE HANDELSRECHT UND WIRTSCHAFTSRECHT (ZHR) 325 (1990).

[64] The great reform of German private international law of 1986 left the area of company law untouched. Even today this area is purely case law.

[65] For 50 years already, the so-called *Deutscher Rat für Internationales Privatrecht*, consisting of professors of private international law, advises the justice ministry when it engages in legislative action concerning private international law. At present, the *Deutsche Rat* has formed a sub-commission which is about to elaborate recommendations for a future European or - if European action fails - a German private international company law.

[66] GROßFELD is the commentator of the section *Internationales Gesellschaftsrecht* (international company law) (13th ed., 1998) in the so-called *Staudinger*, the largest commentary on the German *Bürgerliches Gesetzbuch* (BGB) and its ancillary laws.

[67] EBENROTH was the commentator of the section on *Internationales Gesellschaftsrecht* (international company law) (2nd ed., 1990) in the so-called *Münchener Kommentar zum BGB*, another one of the standard commentaries on German private law, perhaps in practice even more influential than the *Staudinger* (see *supra* note 44).

[68] KINDLER took over EBENROTH's work for the 3rd edition of the *Münchener Kommentar zum BGB* which appeared in 1999, shortly after *Centros*.

lar tried to argue even after *Überseering* and *Inspire Art* that the real seat theory had remained untouched[69]. Lower courts followed him in the time-span between *Centros* and *Überseering* and even improperly denied their duty under Art. 243 TEC to refer their cases to the ECJ[70].

From the viewpoint of the theory of regulatory competition, one can possibly explain the legislator's inactivity by the fact that German company law, highly regulated as it was, would probably have been one of the losers when company founders were allowed to freely choose the place of incorporation and thus the applicable law. On the other hand, the German legislator could not expect to gain anything substantial by engaging in regulatory competition. According to Germany's international tax law, corporate tax is linked to the real seat of the company's enterprises, not to the statutory seat[71]. A franchise tax which would be linked to the fact of incorporation is, first, prohibited within the EU by the 1968 directive on company taxes[72], and secondly, necessarily too low to be of any significance in a state as large as Germany.

Studies on charter competition have shown, that the size of a state taking part in such competition is of primary importance.[73] In a small state like Delaware the franchise tax income may reach a size of 20% or more of the overall budget[74], a figure that is clearly significant for legislative decisions. Yet, the same absolute amount will mean a neglectable share of the budget in a large state like New York or California. In addition, comparatively large states like Germany, while they have little to gain from engaging in regulatory competition, have much to loose. They have to look primarily to the interests of their voters who are mostly employees

---

[69] Peter Kindler, *Internationales Gesellschaftsrecht am Scheideweg*, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 649 (2000); id., *Niederlassungsfreiheit für Scheinauslandsgesellschaften*, NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 1993 (1999); id., *Auf dem Weg zur Europäischen Briefkastengesellschaft? – Die „Überseering"-Entscheidung des EuGH und das internationale Privatrecht*, NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 1073 (2003), id., *„Inspire Art" – Aus Luxemburg nix Neues zum internationalen Gesellschaftsrecht*, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 1086 (2003).

[70] See *supra* note 19.

[71] See more closely EVA-MARIA KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT 184 et seq. (2002).

[72] O.J. EC L 249/25 of 10/3/1969.

[73] See Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, in: HOPT/KANDA/ROE/WYMEERSCH/PRIGGE (eds.), COMPARATIVE CORPORATE GOVERNANCE (1998) p. 143, 175; ID., THE GENIUS OF AMERICAN CORPORATE LAW (1993) p. 7 et seq.

[74] See the figures presented by ROMANO, note 73.

and creditors of companies, not directors. National protective policies however, are evidently endangered by the freedom to choose a lower level of regulation, as it exists in company law matters under the incorporation theory. It is therefore understandable that the German legislator retained the real seat theory as long as possible and did not risk the possibility of a mass exit of German companies, be it to escape codetermination or minimum capital requirements or a corporate law that is often regarded as over-regulatory.

Smaller states, e.g. the Netherlands, which are quite successful in attracting holding companies, have had more incentives to switch to the incorporation theory, which they did in the late 1950's but, confronted with a massive flight of small and medium sized companies, the Dutch legislator still introduced the pseudo-foreign corporation statute of 1997 that was the subject matter of *Inspire Art*. One must, however, admit, that the theory that has just been outlined can hardly explain the development (or rather stagnation) of private international law in Liechtenstein. Although Liechtenstein derives a large share of its state income from incorporation taxes and, already in the 1920's, promulgated an extremely permissive corporate law in order to attract capital, it was only in 1997 that Liechtenstein switched to the incorporation theory.[75]

2. European legislation

Why was it not possible to introduce the incorporation theory by a European legislative act or - before the Treaty of Amsterdam - by an international treaty between the Member States? Why was the treaty of 1968 on the recognition of foreign companies never ratified? Why did the EU attempt to enable companies to move their seat across intra-community borders only in 1997, when it published its first proposition for a 14th directive, and why has the Commission - 5 years after *Centros* - not even been able to issue a new proposition but only a consultation paper[76]? I am afraid that there are more questions than answers.

In 1968, the EEC, as it then was, consisted of only six Member states (Germany, France, Italy, Belgium, Netherlands, Luxemburg), of which all but the Netherlands

---

[75] Before 1/1/1997 Liechtenstein followed the real seat theory, See FÜRSTLICH LIECHTENSTEINISCHER OBERSTER GERICHTSHOF, decision of 11/1/1991, LIECHTENSTEINISCHE ENTSCHEIDUNGSSAMMLUNG 1/1992, 29. See also Guido Meier, *Grundstatut und Sonderanknüpfung im IPR des liechtensteinischen Gesellschaftsrechts* (1979) *passim*, and Peter Prast, *Anerkennung liechtensteinischer Gesellschaften im Ausland* (1997) p. 173. In the course of a general reform and codification of Lichtenstein's private international law, the rules with respct to company law were altered. The new rule (Art. 232 s. 1 Personen- und Gesellschaftsrecht, in force since 1/1/1997) embodies the theory of incorporation.

[76] See *infra* note 88.

followed the real seat theory. Nevertheless, the Treaty of 1968 was based on the incorporation principle, but it allowed the state where the real seat of a company was situated to apply certain mandatory rules. After 1973, the United Kingdom and Ireland disagreed with that solution and the whole project was effectively dead and buried. After *Daily Mail*, Member States like Germany who saw their views supported by the ECJ, were not prepared to give up the real seat theory. Therefore, the 1997 proposition for a 14th directive started from a parallel existence of the real seat and the incorporation theory. Needless to say, since *Centros*, this approach must be seen as clearly outdated. Understandably, the Commission waited for the next, imminent decisions of the ECJ (*Überseering* and *Inspire Art*) before taking action, but it is hard to tell, why - in contrast to its own announcements - the Commission has not yet gone beyond its 2004 consultation document.

3. European Court of Justice

Why did the ECJ in its *Daily Mail* decision, where private international law was clearly not an issue, declare that the freedom of establishment had no influence on the applicability of the Member States' company law, thus depriving art. 43, 48 TEC of their immediate application, something that was clearly contrary to the ECJ's case law on other fundamental freedoms? And why did the same Court, only eleven years later, when company law harmonization had hardly moved forward, decide in the opposite direction, in a case where no real mobility was at stake but the freedom of the incorporators to choose the applicable law?

It is much easier to find possible explanations for *Centros* than for *Daily Mail*. In contrast to the decision itself, the Advocate General's opinion in *Centros* was quite outspoken: He interpreted the freedom of establishment as the freedom of the incorporators to choose the company law that best suits their needs[77] and he openly uttered his doubts about the suitability of minimum capital rules for the protection of corporations' creditors[78]. One might argue that *Centros* was not the most adequate case to overrule *Daily Mail* and to establish the immediate applicability of Art. 43, 48 TEC, because it only involved fictitious mobility. But perhaps the judges were simply not prepared to wait for another 10 or more years before a more suitable case would be referred to them.

By way of contrast, *Daily Mail* s more difficult to explain. On its face and merits, *Daily Mail* was a tax case, not a case on private international law with regard to the

---

[77] Conclusions of the Advocate General M. ANTONIO LA PERGOLA, presented on 16th July 1998, Case C-212/97, *Centros ltd./Erhvervs- og Selskabsstyrelsen*, para. 20.

[78] *Supra* note 77, para. 21.

free movement of companies. Moving the real seat of the company from England to the Netherlands was perfectly possible from the point of view of both English and Dutch conflicts law. The company simply remained an English limited company. The *obiter dictum* on conflicts[79] was perhaps inspired by the wish to include a clarifying word in the ongoing debate about the TEC's impact on conflicts law in company law matters and to shift responsibility away from themselves to the European legislator where it really belonged. However, eleven years later it had become clear that the Member States were unable to find the necessary solution in a timely fashion. Maybe, in *Centros*, the judges felt the need to take the lead again, as they had so often done in the past when interpreting and developing the basic freedoms.

C. Re-incorporations in the US and the EU compared

I. Re-incorporations in the US

"Re-incorporation" is not a legal term of art. It denotes the effect of a transaction which leads to a change of the statutory seat without a change of the real seat of a company. In the US, re-incorporations are an everyday transaction. They are the focus of the so-called 'event studies'.[80] However, there is, at least in Europe, little interest in the way in which such re-incorporations are realized. Some authors believe that the possibility to reincorporate was a result of the incorporation theory.[81] This is not true. According to the incorporation theory, a company's corporate seat cannot be changed. In the debate between real seat and incorporation theory, the stability of the connecting factor has always been regarded as one of the main advantages of the incorporation theory. In fact, re-incorporations are carried out by founding a new (shell) company in the target state and merging the reincorporating company into the new one[82]. The costs for this transaction are not marginal, but they are also not prohibitively high[83]. Contrastingly, as will be shown in the next paragraph, re-incorporations within the EU are hardly possible.

---

[79] Supra note 16, para. 23.

[80] See *supra* note 8.

[81] See THOMAS LUCHSINGER, DIE NIEDERLASSUNGSFREIHEIT DER KAPITALGESELLSCHAFTEN IN DER EG, DEN USA UND DER SCHWEIZ 168 (1992).

[82] ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW 34 et seq. (1993); Alfred F. Conard, in: International Encyclopedia of Comparative Law, vol. XIII: Business and Private Organizations, ch. 6: Fundamental Changes in Marketable Share Companies 14 (1972); Ronald J. Daniels, *Should Provinces Compete? The Case for a Competitive Corporate Law Market*, 36 MCGILL L.J. 131, 178 Fn. 111 (1991).

[83] For more detail, see Roberta Romano, *Law as a Product, Some Pieces of the Incorporation Puzzle*, 1 J.L.ECON.ORG. 225, 246 et seq. (1985).

II. Re-incorporations in the EU

Under conflicts rules in the EU Member States, a change of the statutory seat is neither feasible under the incorporation theory nor under the real seat theory[84]. Only Switzerland and Liechtenstein, which both follow the incorporation theory, have special rules on re-incorporations in the sense of a change of the statutory seat only. But interestingly, according to Art. 162 (1) of the Swiss Law on Private International Law, a foreign company that wishes to reincorporate in Switzerland must also move its real seat to Switzerland. The reason will be that in the absence of a franchise tax, Switzerland will only profit from re-incorporations if the real seat is transferred as well[85]. Contrastingly, Liechtenstein, while drawing considerable income from a tax that comes close to the US franchise tax [86] - offers the possibility to reincorporate without moving the company's real seat to its territory.

It was certainly the main purpose of the 14th directive as proposed in 1997, to enable companies to move their real seat with or without their statutory seat. Whether an isolated change of the statutory seat could also be accomplished under the proposed directive was a matter of some debate[87]. Yet *Centros* rendered the 1997 proposal irrelevant. In March 2004, the Commission published the already referred to consultation document[88] in preparation of a new proposal for a 14th directive. The purpose of the new instrument is somewhat unclear. On the one hand, the Commission expresses its intention to concentrate on the change of the statutory seat rather than the real seat since it deems the latter problem as solved in light of the ECJ's case law. Under para. 2.2. of the consultation document, the Commission even says that the freedom to benefit from a more favourable company law, acknowledged by *Centros* could also be extended to existing companies. Whereas the latter statement points in the direction of allowing re-incorporations, other parts of the paper go in a different direction. In the preamble, the paper says that the pri-

---

[84] See CHRISTOPH WETZLER, *Rechtspolitische Herausforderungen*, in: OTTO SANDROCK & CHRISTOPH WETZLER (eds), DEUTSCHES GESELLSCHAFTSRECHT IM WETTBEWERB DER RECHTSORDNUNGEN, 150 (2004).

[85] See in greater detail EVA-MARIA KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT 155 (2002).

[86] In 1998, Liechtenstein derived 15 % of its total tax income from the so-called "special company tax", see EVA-MARIA KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT 187 (2002).

[87] See EVA-MARIA KIENINGER, WETTBEWERB DER PRIVATRECHTSORDNUNGEN IM EUROPÄISCHEN BINNENMARKT 161 et seq. (2002).

[88] See at http://europa.eu.int/comm/internal_market/company/seat-transfer/index_en.htm (last visited 5 March 2005).

mary purpose of the future directive is to enable companies to adapt their location or their structure to the development of markets and to the development of their position within those markets[89]. And in para. 3.3., the paper leaves it to the Member States to decide whether they make it a prerequisite of the change of the statutory seat that the real seat is also moved to the new state of incorporation. It can be expected that most states will opt for this possibility, since they have little or nothing to gain from attracting only statutory seats of companies.[90]

After legislative bases for re-incorporations have not yet materialized, one may finally ask whether the ECJ's case law does enable existing companies to change their statutory seat.Nothing in the existing decisions points in that direction. *Centros* and *Inspire Art* concerned incorporation decisions, not re-incorporations. In *Überseering*, the Court held that Member States had to accept companies as they were founded in their country of origin, even if they later moved their real seat. Again, a re-incorporation was not at stake. On the contrary, the Court emphasized that the statutory seat was not subject to change, not even when the real seat is moved. In addition, one should not lose sight of the fact, that art. 43, 48 TEC primarily have the purpose to guarantee real and not fictitious mobility. For the time being, it therefore seems safe to conclude that a change solely of the statutory seat is not possible within the EU. In addition, it is not a subject of discussion despite the Commission's consultation paper on a 14th directive and the wealth of publications on charter competition that have appeared after *Centros*[91].

The picture does not change greatly if one also considers re-incorporation mergers. Apart from very recent instances[92] that can still be regarded as exceptional, transnational mergers are not yet a reality in the EU. In private international law it is settled that the law applicable to each of the merging companies (now to be determined by the law of incorporation) also applies to the prerequisites and the proce-

---

[89] See also Stefan Leible, *Niederlassungsfreiheit und Sitzverlegungsrichtlinie*, ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT (ZGR) 531, 554 (2004), in whose opinion the primary economic justification for allowing an isolated change of the statutory seat are those situations where a company has already moved or is planning to move its real seat as well.

[90] See *supra* at note 73 and *infra* at IV.

[91] See e.g. OTTO SANDROCK, Was ist erreicht? Was bleibt zu tun? Eine kollisions- und materiellrechtliche Bilanz, in: OTTO SANDROCK & CHRISTOPH WETZLER (eds.), DEUTSCHES GESELLSCHAFTSRECHT IM WETTBEWERB DER RECHTSORDNUNGEN 77 (2004).

[92] See Jörg-Marcus Leisle, *Transnationale Verschmelzungen im Binnenmarkt: Gelebte Rechtswirklichkeit wird kodifiziert,* THE EUROPEAN LEGAL FORUM 153 (2004); KAI-PETER OTT, *Die rechtsüberschreitende Verschmelzung nach Centros, Überseering und Inspire Art,* in: OTTO SANDROCK & CHRISTOPH WETZLER (eds.), DEUTSCHES GESELLSCHAFTSRECHT IM WETTBEWERB DER RECHTSORDNUNGEN 199, 201 et seq. (2004).

dure of the merger as far as the latter can be determined for each company separately.[93] However, as far as the companies must act together, both laws have to be applied cumulatively.[94] The problem, however, lies in the fact, that most Member States' laws do not provide the necessary substantive law. The German *Umwandlungsgesetz*, for example, deals only with domestic mergers. Some argue that these provisions must be applied by way of an analogy to transnational mergers within the Community. According to this opinion, Member States are obliged to interpret their law so as to be in line with EC-law, here, the freedom of establishment. It is expected, that the ECJ will follow this argument when it will decide on a reference by the *Landgericht* (Regional Court) Koblenz of September, 16, 2003[95]. However, it remains questionable whether the ECJ would apply Arts. 43 and 48 TEC to a transnational intracommunity merger whose sole purpose is a re-incorporation.

The 10th directive on transnational mergers still only exists as a proposal[96]. It contains a minimum of basic rules and leaves all other questions to be determined cumulatively by the applicable national law of the merging companies. One issue among many is the protection of existing creditors. According to Arts. 13 and 14 of the 3rd directive which has harmonised this aspect of national company law, Member States have to introduce adequate guarantees for such existing creditors. Should the 10th directive get passed, one would have to consider the transaction costs in relation to the expected benefits of a change of the applicable law.

By way of conclusion, one can safely state that transnational re-incorporation mergers are not yet practised in the EU.

III. Comparison and conclusion

In the US, re-incorporations are a frequently used method to change the corporate seat after a company has been founded and existed for some time. In practice, re-incorporation in Delaware and similar "responsive" states is far more frequent then

---

[93] Peter Behrens, *Gesellschaft mit beschränkter Haftung* (2nd ed. 1997) para. IPR 69; Christian Bühler, *Die grenzüberschreitende Fusion von Kapitalgesellschaften in der Europäischen Union* (2000) p. 104; Peter Kindler in: *Münchener Kommentar zum Bürgerlichen Gesetzbuch, Vol. 11: Internationales Handels- und Gesellschaftsrecht, Einführungsgesetz zum Bürgerlichen Gesetzbuche (Art. 50-237)*, (3rd ed. 1999), IntGesR para. 668 et seq.; Thomas Ziegler, *Gesellschafts- und steuerrechtliche Probleme der Fusion zwischen deutschen und französischen Aktiengesellschaften* (1997) p. 5 and p. 14.

[94] Kindler (note 93) para. 668; Ziegler (note 93) p. 6.

[95] WERTPAPIER-MITTEILUNGEN (WM) 1990 (2003) = GMBHRUNDSCHAU (GMBHR) 1213 (2003).

[96] Proposal for a Directive of the European Parliament and the Council on Cross-border Mergers of Companies with Share Capital, COM (2003) 703 final.

incorporation because at the start of the life of a company founders hesitate to spend extra money for a corporate domicile that differs from the real seat. It is only later, e.g., when the company goes public, that choosing the law of Delaware or another responsive state becomes an issue. In the model of regulatory competition, reincorporating companies are the "marginal buyers" of "good" corporate law[97]. In relation to the mass of existing corporations, only very few new incorporations take place every year. If only incorporating companies were on the demand side, the threat of competition would be fairly low. It has been argued that the threat that the mass of existing companies could turn their backs to their corporate homes and go elsewhere drives legislative competition[98]. In the EU, until now, this threat is missing. Therefore, a fundamental prerequisite of regulatory competition is still not fulfilled, even after the three *causes célèbres* of the ECJ.

D. Regulatory competition in the EU after *Centros*, *Überseering* and *Inspire Art* - myth or reality?

In the aftermath of the ECJ' s case law, practically everyone who acknowledged the impact of the ECJ's decisions on the real seat theory predicted a start of regulatory competition among the EU-Member States[99]. Such competition would deregulate capital requirements and overcomplicated rules on capital maintenance, it would put an end to co-determination or at least test its asserted economic benefits etc.[100] In short, the "Genius of Corporate Law"[101] would after all make its appearance also in Europe.

---

[97] ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW 32 (1993): *"The key to Delaware's sustained market share over time involves the marginal consumers in the charter market, reincorporating firms"*.

[98] Lucian A. Bebchuk, *Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 HARV.L.REV. 1437, 1458 et seq. (1992).

[99] See e.g. Robert Freitag, Der Wettbewerb der Rechtsordnungen im Internationalen Gesellschaftsrecht, EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT (EUZW) 267 (1999); Stefan Grundmann, Wettbewerb der Regelgeber im Europäischen Gesellschaftsrecht - jedes Marktsegment hat seine Struktur, ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT (ZGR) 783 (2001); Walter Bayer, Die EuGH-Entscheidung "Inspire Art" und die deutsche GmbH im Wettbewerb der europäischen Rechtsordnungen, BETRIEBSBERATER (BB) 2357 (2003); Gerald Spindler & Olaf Berner, Inspire Art - Der europäische Wettbewerb um das Gesellschaftsrecht ist endgültig eröffnet, RECHT DER INTERNATIONALEN WIRTSCHAFT (RIW) 949 (2003); see also Sebastian Mock, Harmonization, Regulation and Legislative Competition in European Corporate Law, http://www.germanlawjournal.com/article.php?id=216

[100] On the economic effeciency of co-determination see Elmar Gerum & Helmut Wagner, Economics of Labor Co-Determination in View of Corporate Governance, in: Hopt/Kanda/Roe/Wymeersch/Prigge (eds.), *Comparative Corporate Governance* (1998) p. 341 at 348 et seq.

[101] See the seminal book by Roberta Romano, THE GENIUS OF AMERICAN CORPORATE LAW (1993).

However, it remains doubtful (I) whether such predictions are founded theoretically and (II) whether they have proved to be true in practice within the five years after *Centros*. Admittedly, this time-span is fairly short, so final conclusions on the existence and results of regulatory competition cannot yet be drawn.

I. The model of regulatory competition applied to the EU

To this point, this paper has primarily looked at the demand side of charter competition. But one also needs to take into consideration the "supply" side. There, it is necessary to identify incentives for corporate law makers to react responsively to the needs of corporate decision makers, otherwise corporate mobility only leads to a freedom to choose the applicable law but not to regulatory competition. As *MacIntosh* said more than ten years ago: *"A competitive market for corporate charters requires more than simply a demand for "good" corporate law. It also requires a supply side response, whereby the suppliers of the "product" - in this case corporate law - are responsive to demands for reform and enact changes to the law that please corporate decision-makers. If suppliers are not responsive to demands for corporate law reform, then there is no more a "market" for corporate law reforms than there is a "market" for consumer goods in Russia".*[102]

While certainly much has changed in the meantime with regard to the "market" in Russia, the core message of MacIntosh's observation still holds true. In the US, charter competition is partly[103] driven by the franchise tax revenue and its importance for smaller states like Delaware. In the EU, a comparable tax for the mere fact of incorporation in a certain state does not exist. Moreover, such a tax could not even be introduced in the future (at least not by an autonomous decision of Member States) since it is expressly prohibited by art. 2 (1) and art. 10 lit. a of Directive 69/335/EEC of July 17, 1969[104]. This directive also impedes any attempt of the incorporating state to collect direct income from the fact of incorporation, for example through registration fees that exceed the real cost[105]. The only indirect source of revenue could be found in an expansion of the "incorporation industry" (law firms,

---

[102] Douglas J. Cumming & Jeffrey G. MacIntosh, *The Role of Interjurisdictional Competition in Shaping Canadian Corporate Law: A Second Look*, 20 Int'l Rev. of Law & Econ. 141, 143-4 (2000) (first published as 18 TORONTO LAW AND ECONOMICS WORKING PAPER SERIES, 1993).

[103] Another factor is the "incorporation industry", i.e. financial and legal services, which are an important branch of the economy in Delaware and similar states.

[104] *Supra* note 72.

[105] Cases C-71/91 and C-178/91, *Ponente Carni Spa et al. v. Amministrazione delle finanze dello stato*, decision of 4/20/1993, E.C.R. I-1915, paras. 41-43 (1993); case C-188/95, *Fantask A/S et al. v. Industriministeriet (Erhvervsministeriet),* decision of 12/2/1997, E.C.R. I-6783 (1997); case C-56/98, *Modelo SGPS SA v. Direcção-Geral dos Registos e Notariado,* decision of 9/29/1999, E.C.R. I-6427 (1999).

accountants, financial businesses). One might also think of non-monetary motivations of legislators, such as the fear that one's own corporate law may become meaningless by massive exit decisions. However, in the existing charter competition literature, such "idealistic" motives play hardly any role.

From a theoretical standpoint, one may conclude that even after the introduction of the incorporation theory, charter competition will hardly take place in the EU, first, because on the demand side, only incorporating but not reincorporating firms have a realistic exit option, and secondly, on the supply side, direct revenues for the incorporating state are excluded by the corporate tax Directive.

II. Does regulatory competition happen and - if yes - where?

As stated earlier, regulatory competition goes beyond mere exit decisions and requires a supply side response. In two EU Member States, France and Spain, new, deregulated forms of limited liability companies have lately been introduced. Since 2003, it has been possible, in France, to found a new form of *Société à Responsabilité Limitée (S.A.R.L.)* within 24 hours and with a nominal minimum capital of 1 Euro (the normal minimum capital for a *S.A.R.L.* is € 7500-)[106]. The formalities of incorporation are reduced to a minimum, even applications for registration via internet become possible; founders can seek the assistance of a *Centre de Formalités des Entreprises*. The legislation includes facilitations in other areas: the newly founded company enjoys certain reductions of tax and social contributions within the first years of its existence and may use the private address of the founder as the corporate seat even where this would otherwise be contrary to rental contracts or general city planning legislation. In sum, the main purpose of this new legislation is to encourage small start-up enterprises that have their real seat and their main field of activity in France. The "*Blitz-SARL*" as it has been baptized, has not been introduced with a view to attract incorporations from abroad. Largely similar legislation has existed in Spain since April 1, 2003[107]. In contrast to French law, the Spanish *Sociedad Limitada Nueva Empresa* must have a minimum nominal capital of 3012.- €; interestingly, the new legislation also fixes a maximum nominal capital of 120.200.- €.[108] Like the French *Blitz-GmbH*, the "*nueva empresa*" is designed to encourage and support small and medium sized start-up enterprises located in Spain.[109] In the preparatory documents, there is not the slightest hint that the Spanish legislator passed the new legislation in order to take part in charter competition.[110]

The notion of regulatory competition is only to be found in the currently ongoing company law reform in the United Kingdom.[111] It is one of the explicit goals of the

---

[106] See Patrizia Becker, *Verabschiedung des Gesetzes über die französische Blitz-S.A.R.L.*, GMBHRUNDSCHAU (GMBHR) 706 (2003) and GMBHRUNDSCHAU (GMBHR) 1120 (2003).

[107] See Nadja Vietz, *Verabschiedung des Gesetzes über die neue Blitz-GmbH*, GMBHRUNDSCHAU (GMBHR) 26 (2003) and GMBHRUNDSCHAU (GMBHR) 523 (2003); José Miguel Embid Irujo, *Eine spanische "Erfindung" im Gesellschaftsrecht: Die "Sociedad limitada nueva empresa" - die neue unternehmerische GmbH*, RIW 760 (2004); Sebastian Cohnen, *Kein GmbH-rechtliches „race to the bottom" auf dem Jakobsweg: Bemerkungen zur neuen Rechtsform der S.L.N.E.*, ZVGLRWISS (forthcoming).

[108] Embid Irujo, *supra* note 107, at 764.

[109] Embid Irujo, *supra* note 107, at 761.

[110] See Cohnen, *supra* note 107.

[111] The consultation documents are published under www.dti.gov.uk/cld/reviews/condocs.htm (last visited 5/4/2005).

reform process to make the UK even more attractive as a corporate home for overseas companies[112]. Because London is already the most important financial centre within the EU it seems plausible that the indirect benefits which the UK may draw from strengthening its financial services sector are considerable enough to drive corporate law legislators; taken negatively, the UK has much more to lose in this respect than other Member States. However, one will have to wait until the reform process is closed in order to judge from the results whether charter competition has in fact taken place.

To answer the question stated in the title of this part, it is suggested that charter competition in the EU is still a myth. The chances for a change in the future are unclear. From a theoretical point of view, it seems more than doubtful that something similar to the "race" that took place in the late 19th and the beginning of the 20th century in the US will happen in the EU. What is happening is that a considerable number of small and medium sized enterprises are choosing to incorporate in the UK rather than under German law. The main reason is the minimum capital requirement for a German GmbH of € 25.000.-. This movement began in the immediate aftermath of *Überseering* and it is impossible to foresee whether the trend will persist or whether negative experiences (higher costs for expert advice on foreign law, liability for fraudulent or wrongful trading under UK law, potential applicability of certain German tort and insolvency law provisions despite incorporation in the UK) will produce a chilling effect.

It is also important to note that all the developments described are occurring only with respect to small sized, privately held companies. Publicly held, listed companies are not affected, neither by possible faint signs of regulatory competition nor by the exit movement. There are a number of explanations: First and foremost, harmonisation of EU corporate law primarily addresses publicly held companies, so that there is little space for national deviations in this area. Second, from a German point of view, the problem of co-determination is still unsolved; it is an open question whether the ECJ will consider the protection of co-determination as a mandatory requirement in the public interest. Third, the transaction costs of incorporating in a Member State which is not the real home of the company is probably much higher in the EU than in the US. In the US, a well-qualified corporate lawyer will know the law of Delaware, even if she works and resides in another state. In contrast, in the EU, competence in foreign laws that goes beyond registration formalities and a comparison of minimum capital sums is likely to be limited to lawyers in a few large and expensive law firms . For these reasons, practitioners do not

---

[112] See White Paper Company Law Reform (March 2005), http://www.dti.gov.uk/cld/WhitePaper.pdf, p. 9.

expect large companies to incorporate outside the state in which they primarily conduct their business[113]. Even the present attractiveness of the English limited company for corporations based in Germany is not expected to last for a long time[114].

In sum, there is a marked contrast between the EU and the US, because in the US, charter competition is primarily happening (and being examined) with respect to large, publicly held companies, whereas the main field of the so-called charter competition in the EU (which presently is only a use of the freedom of choice of law but without any supply side reaction) is the small sized company whose founders want to save a few thousand Euros minimum capital.

E. Summary

Although the Member States - under the compulsion of the ECJ's jurisprudence - now follow the incorporation theory, the two main prerequisites for charter competition are not yet fulfilled within the EU. On the demand side, the new mobility only extends to incorporating companies, not to reincorporating ones. In fact, European legislators and academic writers seem not yet to have grasped the central role of re-incorporations for the functioning of regulatory competition, since, despite the flood of publications on the new framework of charter competition in Europe, the issue of re-incorporation is not discussed. On the supply side, robust advantages of attracting incorporations are missing because of the 1969 companies' tax directive. More indirect or subtle advantages may exist but until now, signs of supply side responses are not visible. To conclude, regulatory competition in company law in the EU is still a myth, not a reality.

---

[113] Roger Kiem, *Das Centros-Urteil des Europäischen Gerichtshofs – Praktische Gestaltungs- und Reaktionsmöglichkeiten aus dem Blickwinkel der Gesellschaften*, in: GESELLSCHAFTSRECHTLICHE VEREINIGUNG (ed.), GESELLSCHAFTSRECHT IN DER DISKUSSION 1999, at 199, 210 et seq. (2000).

[114] Alexander Hirsch & Richard Britain, *Artfully Inspired - Werden deutsche Gesellschaften englisch?*, NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT (NZG) 1100, 1103 et seq. (2003).