



Making the Case for a *Rome V Regulation on the Law Applicable to Companies*

Law Working Paper N° 549/2020
October 2020

Carsten Gerner-Beuerle
University College London and ECGI

Federico M. Mucciarelli
University of Modena and Reggio Emilia and
SOAS University of London

Edmund Schuster
London School of Economics and Political Science

Mathias Siems
European University Institute, Durham University,
and ECGI

© Carsten Gerner-Beuerle, Federico M. Mucciarelli,
Edmund Schuster and Mathias Siems 2020. All
rights reserved. Short sections of text, not to exceed
two paragraphs, may be quoted without explicit per-
mission provided that full credit, including © notice,
is given to the source.

This paper can be downloaded without charge from:
http://ssrn.com/abstract_id=3720574

<https://ecgi.global/content/working-papers>

European Corporate Governance Institute

ECGI Working Paper Series in Law

Making the Case for a
*Rome V Regulation on the Law Applicable to
Companies*

Working Paper N° 549/2020

October 2020

Carsten Gerner-Beuerle
Federico M. Mucciarelli
Edmund Schuster
Mathias Siems

Abstract

There is significant legal variation and uncertainty in the conflict of laws rules applicable to companies in the EU. While the case law of the Court of Justice on the freedom of establishment has clarified some questions, it is evident that case law cannot provide for an adequate level of legal certainty. The main recommendation of this paper is that private international company law in the EU should be harmonised. The paper discusses the main challenges that a future regulation to this effect – called here ‘Rome V Regulation on the Law Applicable to Companies’ – would have to overcome. Some of those are of a political nature: for instance, countries may fear that it may become easier for companies to evade domestic company law (eg, rules of employee co-determination), and there are specific considerations that concern companies established in third countries. Another challenge is that a future regulation on the law applicable to companies has to be consistent with existing EU conflict of laws rules as regards, for example, insolvency and tort law, while also complying with the freedom of establishment of the Treaty. It is the aim of this paper to discuss these questions in detail, notably the general considerations for harmonisation in this field, a potential harmonisation based on the ‘incorporation theory’, how it may be possible to overcome some contentious issues such as the definition of the *lex societatis* or the relationship between the *lex societatis* and other areas of law, and the prospects of future international harmonisation.

Keywords: freedom of establishment, private international law, *lex societatis*, harmonisation

JEL Classifications: G38, K22, K31, K33, M13

Carsten Gerner-Beuerle
Professor of Commercial Law
University College London, Faculty of Laws
Gower Street
London, WC1E 6BT, United Kingdom
e-mail: c.gerner@ucl.ac.uk

Federico M. Mucciarelli
Professor of Business Law
University of Modena and Reggio Emilia,
Viale Berengario 51
41100 Modena, Italy
phone: +39 592 056 778
e-mail: federicomaria.mucciarelli@unimore.it

Edmund Schuster
Associate Professor of Law
London School of Economics and Political Science, Department of Law
54 Lincoln's Inn Fields
London WC2A 3LJ, United Kingdom
phone: +44 207 955 7452
e-mail: E.Schuster@lse.ac.uk

Mathias Siems*
Professor of Private Law and Market Regulation, Professor of Commercial Law
European University Institute, Department of Law
Via Bolognese 156
50139 Florence, Italy
phone: +39 554 686 544 306
e-mail: Mathias.Siems@EUI.eu

*Corresponding Author

Making the Case for a

Rome V Regulation on the Law Applicable to Companies

Carsten Gerner-Beuerle,* Federico Mucciarelli,**

Edmund Schuster,*** Mathias Siems****

Abstract: There is significant legal variation and uncertainty in the conflict of laws rules applicable to companies in the EU. While the case law of the Court of Justice on the freedom of establishment has clarified some questions, it is evident that case law cannot provide for an adequate level of legal certainty. The main recommendation of this paper is that private international company law in the EU should be harmonised. The paper discusses the main challenges that a future regulation to this effect – called here ‘Rome V Regulation on the Law Applicable to Companies’ – would have to overcome. Some of those are of a political nature: for instance, countries may fear that it may become easier for companies to evade domestic company law (eg, rules of employee co-determination), and there are specific considerations that concern companies established in third countries. Another challenge is that a future regulation on the law applicable to companies has to be consistent with existing EU conflict of laws rules as regards, for example, insolvency and tort law, while also complying with the freedom of establishment of the Treaty. It is the aim of this paper to discuss these questions in detail, notably the general considerations for harmonisation in this field, a potential harmonisation based on the ‘incorporation theory’, how it may be possible to overcome some contentious issues such as the definition of the *lex societatis* or the relationship between the *lex societatis* and other areas of law, and the prospects of future international harmonisation.

Keywords: freedom of establishment, private international law, *lex societatis*, harmonisation

JEL Classification: G38, K22, K31, K33, M13

* Professor of Commercial Law, University College London, UK, and ECGI Research Member.

** Professor of Business Law, University of Modena and Reggio Emilia, Italy.

*** Associate Professor of Law, London School of Economics and Political Science, UK.

**** Professor of Private Law and Market Regulation, European University Institute, Italy, Professor of Commercial Law, Durham University, UK (on leave), and ECGI Research Member.

A revised version of the paper will be published in the [Yearbook of European Law](#).

I. Introduction

The case law of the Court of Justice on the Treaty's freedom of establishment as applied to companies (*Daily Mail*, *Centros* etc) is a core topic of major books on EU law.¹ In the literature on conflict of laws (private international law), any book published in Europe refers to the 'Rome regulations' enacted since 2008.² This paper aims to bring together these two important topics. It is part of a wider project that has discussed the law applicable to companies from a European, comparative and empirical perspective;³ yet, this is the first paper of this series that explicitly addresses the normative question about the feasibility of a future EU regulation on the topic.

This paper suggests that there is a case to be made for a 'Rome V Regulation on the Law Applicable to Companies'⁴ as the next milestone for a comprehensive legislative framework on EU private international law. As this paper will explain, there are some indications that the EU Commission may take up this topic. Moreover, the UK's departure from the EU can be seen as an occasion to tackle the harmonisation of conflict of laws rules applicable to companies, as the remaining 27 Member States may now want to decide whether a formal regulatory framework should be put in place to facilitate (or impede) the emergence of one or more other Member States as primary destinations of foreign incorporations.⁵

In substance, the main argument in favour of harmonisation is that the case law of the Court of Justice has not led to the legal certainty necessary for companies, their creditors and society as a whole.⁶ Yet, this paper will also discuss that any future regulation has to overcome a number of challenges. Some of those are of a political nature: for instance, some countries may fear that it may become easier for companies to evade domestic company law,

¹ Eg, Damian Chalmers, Gareth Davies and Giorgio Monti, *European Union Law* (4th edn, Cambridge: Cambridge University Press 2019), 810–7; Robert Schütze, *European Union Law* (2nd edn, Cambridge: Cambridge University Press 2018), 620–34.

² Eg, Peter Stone, *Stone on Private International Law in the European Union* (4th edn, Cheltenham: Edward Elgar 2018); Geert van Calster, *European Private International Law* (2nd edn, Oxford: Hart Publishing 2016).

³ See the references in Section III.A, below.

⁴ The numbering would follow on from: Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations ('Rome I'); Regulation (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations ('Rome II'); Regulation (EU) No 1259/2010 of 20 December 2010 implementing enhanced cooperation in the area of the law applicable to divorce and legal separation ('Rome III'); Regulation (EU) No 650/2012 of the European Parliament and of the Council of 4 July 2012 on jurisdiction, applicable law, recognition and enforcement of decisions and acceptance and enforcement of authentic instruments in matters of succession and on the creation of a European Certificate of Succession ('Rome IV'). Note that the designations 'Rome III' and 'Rome IV' are not part of the official title of these regulations but widely used in the literature.

⁵ The question whether there could be a 'Delaware effect' in the EU has been a frequent topic in the literature; see Section III.B.(ii), below. .

⁶ For legal certainty as an overarching principle of EU law see Takis Tridimas, *The General Principles of EU Law* (2nd edn, Oxford: Oxford University Press 2007), 242–51. For a comparative analysis of legal certainty see Mark Fenwick, Mathias Siems and Stefan Wrbka (eds), *The Shifting Meaning of Legal Certainty in Comparative and Transnational Law* (Oxford: Hart Publishing 2017).

in particular for companies established in third countries. A further key challenge is that a future regulation on the law applicable to companies has to be clear on how it would relate to existing EU conflict of laws rules as regards, for example, insolvency and tort law, while also being in compliance with the freedom of establishment of the Treaty.

This paper is structured as follows. To set the scene, Section II outlines the status quo of relevant EU case law and legislation and Section III presents general considerations for harmonisation in this field. Section IV then turns to the core issue of a possible harmonisation based on the ‘incorporation theory’, discussing the most relevant issues in some detail (though without claiming to be exhaustive⁷). Section V concludes.

II. Status quo of relevant EU case law and legislation

A. Freedom of establishment and case law on corporate mobility

Companies, different from natural persons, exist only by virtue of a legal system, which regulates their formation and internal affairs; thus, in principle, we can say that companies are made of rules and that such rules are established at the national level.⁸ In the EU, company law is predominantly a matter of domestic law.⁹ Conflict of laws rules determining the law applicable to companies (*lex societatis*) are also determined at the Member State level. The main divide in the law applicable to companies is between the ‘incorporation theory’ and the ‘real seat theory’. This division cannot capture all nuances of national regimes, and countries may in practice follow diverging solutions regarding specific legal questions.¹⁰ Nevertheless, a binary classification can capture the general approach of the private international law of a country towards foreign legal entities. In particular, countries that follow the ‘incorporation theory’ generally recognise any company properly constituted according to the law of another country and accept that the company law of the country of incorporation applies to such companies. By contrast, countries following the ‘real-seat theory’ seek to inhibit the free choice of company law by determining the law applicable to a company by reference to the

⁷ Special emphasis will be put on the scope of a future regulation (as regards the relationship to other areas of law but also geographically); other relevant topics, not discussed here in detail, include the mechanisms to protect public interests (*ordre public* and overriding mandatory provisions).

⁸ See eg Massimo Benedettelli, ‘Five Lay Commandments for the EU Private International Law of Companies’ (2015/16) 17 *Yearbook of Private International Law* 209; Louis d’Avout, *L’entreprise et les conflits internationaux de lois* (Collected Course of the Hague Academy of International Law, vol. 38, 2019). Few supranational forms of companies exist, such as the Societas Europaea (SE).

⁹ See eg Luca Enriques, ‘A Harmonized European Company Law: Are We There Already?’ (2017) 66 *International and Comparative Law Quarterly* 763; Luca Enriques, ‘EC Company Law Directives and Regulations: How Trivial Are They?’ (2006) 27 *University of Pennsylvania Journal of International Economic Law* 2.

¹⁰ Benedettelli (n 8), 217–8.

location of its headquarters; this effectively requires companies to incorporate in the jurisdiction from where they are managed.¹¹

The case law of the Court of Justice interpreting the freedom of establishment of Articles 49, 54 of the Treaty of the Functioning of the European Union (TFEU) (and its predecessors) has, however, led to some liberalisation regarding the freedom of selecting the preferred *lex societatis*.¹² Although the Court generally does not phrase its arguments in the categories of conflict of laws rules, it has become clear that its case law has imposed restrictions on the use of the real seat theory for companies from other Member States.

In the landmark case of *Centros*, for example, two Danish citizens living in Denmark established a limited liability company (ltd) in the UK. The founders' main motivation was to avoid minimum capital requirements under Danish law. Even though it is somewhat unclear whether Denmark followed the real seat doctrine at the time, the Danish authorities refused to register a branch of Centros ltd in the commercial register because it did not plan to conduct business anywhere except in Denmark. The Court of Justice rejected this line of reasoning and held that Centros ltd was validly exercising its freedom of establishment and that the refusal to register was an obstacle to this freedom. However, the Court also affirmed that Denmark was 'entitled to take measures designed to prevent certain of its nationals from attempting, under cover of the rights created by the Treaty, to improperly circumvent their national legislation or to prevent individuals from improperly or fraudulently taking advantage of [the freedoms]'.¹³ Later decisions of the Court of Justice have further expanded on this holding by stating that Member States cannot apply domestic liability rules to legal entities incorporated in other Member States¹⁴ and that such companies must be recognised as legal entities regulated by the country of incorporation.¹⁵

This broad interpretation of the freedom of establishment, as applied to legal entities, can lead to tension. One the one hand, it can be argued that shareholders would seek for the best-tailored company law regime that fits the needs of their business, and that this would trigger a beneficial regulatory competition among Member States. On the other hand, a divergence between the country where the business is situated, and hence typically the most-affected interests are located, and the country that regulates the company might be politically

¹¹ See eg Stephan Rammeloo, *Corporations in Private International Law* (Oxford: Oxford University Press 2001). For its application to the EU context see eg Justin Borg-Barthet, *The Governing Law of Companies in EU Law* (Oxford: Hart Publishing 2012) as well as the references in Section III.A, below.

¹² C-212/97 *Centros Ltd v Erhvervsog Selskabsstyrelsen* [1999] ECR I-1459; C-208/00 *Überseering BV v Nordic Construction Company Baumanagement GmbH* [2002] ECR I-9919; C-167/01 *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art* [2003] ECR I-1095; C-411/03 *SEVIC System AG* [2005] ECR I-10805; C-210/06 *Cartesio Oktató és Szolgáltató bt* [2008] ECR I-9641; C-378/10 *VALE Építési kft*, ECLI:EU:C:2012:440; C-106/16 *Polbud – Wykonawstwo sp. z o.o* [2017] ECLI:EU:C:2017:804.

¹³ *Centros*, ibid, at paras. 24-25.

¹⁴ *Inspire Art* (n 12).

¹⁵ *Überseering* (n 12).

unacceptable when company law rules not only affect intra-corporate affairs, but also aim to protect other stakeholders.¹⁶

In addition, the case law of the Court has emphasised repeatedly that it is possible for Member States to provide that incorporations in their own jurisdiction are tied to the requirement that the company has its headquarters, or other physical elements, in this country. For example, it has stated explicitly that ‘a Member State [is] able, in the case of a company incorporated under its law, to make the company’s right to retain its legal personality under the law of that State subject to restrictions on the transfer of the company’s actual centre of administration to a foreign country.’¹⁷ It derives this result not only from prior case law going ultimately back to *Daily Mail*,¹⁸ but also from the wording of Article 54 TFEU. Given that Article 54 places the registered office, central administration and principal place of business on an equal footing, the Court argues that

‘in the absence of a uniform Community law definition of the companies which may enjoy the right of establishment on the basis of a single connecting factor determining the national law applicable to a company [...] a Member State has the power to define both the connecting factor required of a company if it is to be regarded as incorporated under the law of that Member State and, as such, capable of enjoying the right of establishment, and that required if the company is to be able subsequently to maintain that status.’¹⁹

It follows that this line of cases enables Member States to insist that, in principle, companies formed under their company laws maintain a physical presence, including their headquarters or real seat, in the territory of that Member State as a matter of substantive company law. Similarly, the use by a Member State of any other connecting factor in its conflict of laws rules falls outside the scope of the Treaty, provided it is used only in relation to companies claiming their status under that Member State’s laws.²⁰

¹⁶ Lynn M LoPucki, ‘Corporate Charter Competition’ (2018) 102 *Minnesota Law Review* 2101, 2137-40.

¹⁷ *Überseering*, para 70, confirmed in *Cartesio*, para 107.

¹⁸ C-81/87 *The Queen v H.M. Treasury and Commissioners of Inland Revenue ex parte Daily Mail and General Trust plc* [1998] ECR I-5483, in this regard, confirmed in *Cartesio* and *VALE*.

¹⁹ *Cartesio*, paras 109-110.

²⁰ See eg *Überseering*, para 70, and *Cartesio*, para 107, both of which primarily seem to have a conflict of laws rule in mind based on context.

B. The Company Law Package and its limitations

In May 2017, the EU Commission conducted a consultation on the theme ‘EU Company law upgraded: Rules on digital solutions and efficient cross-border operations’.²¹ In April 2018, this was followed by the publication of the so-called Company Law Package, which discussed possible harmonisation of selected fields of substantive company law as well as conflict of laws rules applicable to companies.²² Specifically, with respect to conflict of laws, the Commission’s Impact Assessment endorses EU harmonisation in this field.²³

The Impact Assessment outlines a number of preferred options: first, it suggests that the connecting factor should be determined on the basis of the place of incorporation of the company, while also acknowledging that some specific rules could use the real seat as a connecting factor (eg, for the protection of third parties). Second, it states that as regards the protection of stakeholders in case of a change of the applicable law, the law of the forum shall prevail as far overriding mandatory provisions and public policy consideration are at play. Third, as regards the rules on employee participation at board level, the document states that no uniform conflict of laws, but rather national conflict of laws rules shall apply. Fourth, it is suggested that the territorial scope of application of any harmonised rules should only cover companies established in the EU (not companies from third countries).²⁴

It follows that this document by the EU Commission shows a mixed, if not ambivalent, ambition. On the one hand, it suggests adopting the incorporation theory; on the other hand, it acknowledges a number of limitations to future harmonisation based on such an approach. Moreover, at the very end of the text, the Impact Assessment even seems to backtrack from an immediate harmonisation of conflict of laws rules, stating that:

‘[...] given that the instances in which clarity is most needed, namely specific issues related to the law applicable to limited liability companies in cross-border situations, will be addressed in the proposed legislation on cross-border conversions, mergers and divisions, it was decided not to propose a specific legislative act on conflict-of-laws at this point in time.’

In 2019, the EU then adopted a directive that addresses cross-border conversions, mergers and divisions.²⁵ There is also an ongoing evaluation of the use of ‘letterbox companies’

²¹ European Commission, consultation document available at https://ec.europa.eu/info/sites/info/files/eu_company_law_upgraded_public_consultation.pdf.

²² EU Company Law Package, available at https://ec.europa.eu/info/publications/company-law-package_en.

²³ Impact Assessment (SWD/2018/141 final - 2018/0113 (COD)), available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD%3A2018%3A141%3AFIN>.

²⁴ Ibid at pp 75–85.

²⁵ Directive (EU) 2019/2121 of the European Parliament and of the Council of 27 November 2019 amending Directive (EU) 2017/1132 as regards cross-border conversions, mergers and divisions.

which relates to some aspects conflict of laws (as well as other topics).²⁶ Thus, future harmonisation of conflict of laws rules applicable to companies seems to remain on the agenda, motivating the following analysis.

III. General considerations for harmonisation in this field

A. Remaining differences of conflict of laws rules applicable to companies

Despite the case law of the Court of Justice,²⁷ there remain considerable differences in the conflict of laws rules applicable to companies between the Member States. Furthermore, in some instances, the EU requirements that can be derived from the freedom of establishment have not been sufficiently implemented by domestic law-makers. This issue was examined in detail in a ‘Study on the Law Applicable to Companies’,²⁸ a corresponding book²⁹ and journal publications.³⁰ Amongst other issues, the Study explains that the conflict of laws rules of some Member States do not unambiguously refer to the state of incorporation and that some Member States provide for secondary connecting factors that deviate from this principle. Notably, it finds significant variation in the way the relevant connecting factor is formulated and the exceptions to this connecting factor where a foreign company has substantial links to the host state. Some countries still formally adhere to the real seat doctrine, but modify its application. Others apply their domestic law to foreign companies at the choice of third parties if the company’s real seat is located within the host state. Yet others apply specific provisions of their domestic company law (broadly understood) to foreign companies if idiosyncratic links of differing intensity with the host state are present, for example the location of assets in the host state or the carrying on of business activity.³¹

²⁶ See European Commission, Technical Annex to the request for service – JUST/2017/RPPI/FW/CIVI/0173 (2018/04) for Study on letterbox companies, as well as European Parliamentary Research Service, ‘An overview of shell companies in the European Union’ (2018), available at [https://www.europarl.europa.eu/RegData/-etudes/STUD/2018/627129/EPRS_STU\(2018\)627129_EN.pdf](https://www.europarl.europa.eu/RegData/-etudes/STUD/2018/627129/EPRS_STU(2018)627129_EN.pdf). See also Delphine Nougayrède, ‘After the Panama Papers: A Private Law Critique of Shell Companies’ (2019) 52 *International Lawyer* 327.

²⁷ See Section II.A., above.

²⁸ Carsten Gerner-Beuerle, Federico M Mucciarelli, Edmund Schuster and Mathias Siems, *Study on the Law Applicable to Companies* (Report for EU Commission, DG Justice 2017).

²⁹ Carsten Gerner-Beuerle, Federico M Mucciarelli, Edmund Schuster and Mathias Siems (eds.), *The Private International Law of Companies in Europe* (Munich: C.H. Beck 2019).

³⁰ Carsten Gerner-Beuerle, Federico M Mucciarelli, Edmund Schuster and Mathias Siems, ‘The Illusion of Motion: Corporate (Im-)mobility and the Failed Promise of Centros’ (2019) 20 *European Business Organization Law Review* 425; Carsten Gerner-Beuerle, Federico M Mucciarelli, Edmund Schuster and Mathias Siems, ‘Cross-border Reincorporations in the European Union: The Case for Comprehensive Harmonisation’ (2018) 18 *Journal of Corporate Law Studies* 1; Carsten Gerner-Beuerle, Federico M Mucciarelli, Edmund Schuster and Mathias Siems, ‘Why Do Businesses Incorporate in Other EU Member States? An Empirical Analysis of the Role of Conflict of Laws Rules’ (2018) 56 *International Review of Law and Economics* 14.

³¹ Gerner-Beuerle et al (n 28), 15.

Table 1: ‘Incorporation theory score’, showing ‘pureness’ of incorporation theory

Coding	Definition	Countries
1	if a connecting factor based upon the incorporation theory is clearly formulated in legislation or through judge-made law (i.e. in a way that everyone, even non-experts, can grasp it) and no exceptions are provided (i.e. no additional connecting factors based upon the location of a company’s real seat).	Bulgaria, Cyprus, Czech Republic, Finland, Hungary, Ireland, Lithuania, Malta, Netherlands, Slovakia, Sweden, UK
2/3	if (i) a connecting factor based upon the incorporation theory is clearly formulated but this criterion is subject to exceptions, or (ii) legal experts can identify that the country follows a connecting factor based upon the incorporation theory and no exceptions are provided but non-experts are uncertain about this position.	Austria, Belgium, Croatia, Estonia, France, Germany, Italy, Romania, Slovenia, Spain
1/3	as in previous scenario (ii) but exceptions to the incorporation theory clearly exist.	Denmark, Greece, Latvia, Luxembourg
0	scenario where even legal experts cannot identify that the country follows a connecting factor based upon the incorporation theory	Poland, Portugal

One of the previous publications deriving from this Study coded these remaining differences showing the degree of ‘pureness’ of the incorporation theory under rules of conflict of laws, see Table 1.³² It shows that only eleven Member States apply a ‘pure’ version of the incorporation theory. By contrast, in the remaining Member States the situation was found to be less clear, be it because the incorporation theory is subject to exceptions or there is uncertainty as to whether (or how far) the country really applies the incorporation theory.

The aforementioned Study also established that some host states seek to extend the international reach of their laws by providing for exceptional connecting factors or qualifying certain rules as overriding mandatory provisions. This raises questions as to the conformity of such connecting factors and rules with the right of establishment as interpreted by the Court of Justice. In principle, the answer may be derived in each individual case by applying the Court’s *Gebhard*³³ conditions; yet, this is applied inconsistently in the Member States. Furthermore, the delimitation of the international scope of company law and other legal areas was found to be problematic in several respects. Although in some areas of law, notably insolvency, contract and tort law, connecting factors are laid down in instruments of EU law, it is not always clear how these factors are applied, and problems of regulatory gaps or the cumulative application of two or more legal regimes arise where legal mechanisms that

³² Gerner-Beuerle et al (n 30) (*Why Do Businesses Incorporate*), 22. Note that this paper still included the UK as a Member State.

³³ C-55/94 *Reinhard Gebhard v. Consiglio dell’Ordine degli Avvocati e Procuratori di Milano* [1995] ECR I-04165.

perform a similar function but use different legal techniques are classified differently in the Member States.³⁴

B. The need for common rules

(i) Legal certainty

The question of whether the EU should harmonise conflict of laws rules applicable to companies relates to the more general allocation of regulatory power in a ‘multi-layer’ system. In this regard, the preliminary question is whether further harmonisation of substantive company law at the EU level is likely to render harmonisation of conflict of laws rules less relevant. Such harmonisation of substantive law would largely remove legal uncertainty in the area,³⁵ which is mainly a consequence of differences between national company law regimes. However, despite the emergence of European company forms (notably the SE) and ongoing harmonisation measures,³⁶ it is now clear that there is no realistic prospect of anything approximating a uniform EU-wide company law emerging. Given the persistence of diversity in Member State company laws, conflict of laws rules will therefore continue to play a crucial role.

As there is considerable diversity between the Member States as regards conflict of laws rules applicable to companies,³⁷ it is often not clear which company law is applicable. For example, a company that has its place of incorporation and its ‘real seat’ in two different countries may be treated as being subject to different legal rules depending on the conflict of laws rules that a court (of whatever country) may apply. In order to improve legal certainty and predictability, it is therefore, for example, advisable to provide for harmonised rules that clarify the scope of the relevant connecting factor (or factors).³⁸ Such an argument is line with the general aim of conflict of laws (or private international law) to identify the closest relationship in a neutral and certain way.³⁹ In the EU context, this position can also be supported by the freedom of establishment of the Treaty, and – at a more general level – arguments of inter-jurisdictional efficiency (ie the aim is to satisfy the collective demands of

³⁴ See Carsten Gerner-Beuerle and Edmund Schuster, ‘The Costs of Separation: Conflicts in Company and Insolvency Law in Europe’ (2014) 14 *Journal of Corporate Law Studies* 287 as well as Section IV.B, below.

³⁵ Such harmonisation would not completely solve the issue of the law applicable to companies, since companies, as creatures of national law, would still need to derive their status (and existence) from one legal system, even if the content of the rules were identical in all respects.

³⁶ See Section II.B, above, as well as https://ec.europa.eu/info/business-economy-euro/doing-business-eu/company-law-and-corporate-governance_en.

³⁷ See A, above.

³⁸ For details see Section IV, below.

³⁹ For the role of Savigny’s approach to private international law in Europe see also Van Calster (n 2), 4. For a different view see Rammeloo (n 11), 315 (arguing that the ‘the ancient Savignian private international law concept of ascertaining the closest relationship can no longer be used to regulated international company law relationships’).

individuals at minimum cost in all jurisdictions, not simply efficiency in specific jurisdictions⁴⁰).

The Study, mentioned in the previous section, also supports this case for harmonisation with empirical findings. Its analysis of statistical data⁴¹ examined how far, in the EU, companies operate in some form in Member States different from the Member State in which they have been incorporated. It found that, to some extent, such corporate mobility is already a reality. However, it also established that decisions about domestic or foreign incorporations are not merely a result of differences in substantive company law. Using regression analysis, it showed that countries that have a clear-cut version of the ‘incorporation theory’ benefit in this market for incorporations, as compared to countries that have retained elements of the ‘real seat theory’, by attracting a higher number of companies incorporated by foreign business. It also identified a negative effect of existing differences in the conflict of laws rules applicable to companies. Thus, these findings show that the case law of the Court of Justice has not made differences in the conflict of laws rules applicable to companies obsolete and that EU harmonisation could have a positive effect in this area of law.

The Study also included an empirical survey⁴² dealing with the practical problems created by the legal uncertainty for companies stemming from unclear and non-uniform conflicts of laws rules in a context where the substantive laws of the Member States have not been fully harmonised. The main finding of the survey was that there are significant practical obstacles to corporate mobility in the EU. In particular, it is notable that many of the respondents based in Member States that have retained an element of the ‘real seat theory’⁴³ report such practical obstacles. There is also a strong positive correlation between respondents who are critical of the approach of their domestic law and who support EU harmonisation of conflict of laws rules. In addition, an analysis of group differences shows that there is still a divide between the ‘old’ and ‘new’ Member States as respondents from the latter countries are more likely to indicate a lack of familiarity with the relevant procedures and report practical problems in their dealings with domestic courts and commercial registers.

The outcome of the EU consultation leading to the Company Law Package⁴⁴ provides further empirical confirmation of these preferences in favour of harmonisation, in particular due to reasons of legal certainty. Amongst others, it reports that 60% of the national public authorities and business organisations which took part in the consultation took the view that

⁴⁰ For this distinction see Robert P Inman and Daniel L Rubinfield, ‘Economics of Federalism’ in Francesco Parisi (ed) *The Oxford Handbook of Law and Economics: Volume 3: Public Law and Legal Institutions* (Oxford: Oxford University Press 2017).

⁴¹ Gerner-Beuerle et al (n 28), 33–64. An updated version of these findings was published in Gerner-Beuerle et al (n 30) (*Why Do Businesses Incorporate*).

⁴² Gerner-Beuerle et al (n 28), 65–99.

⁴³ See A, above.

⁴⁴ See Section II.B, above.

differences in the laws of the Member States and the lack of EU rules ‘constitute obstacles to the proper functioning of the internal market – with 28% considering it as an obstacle to a large or very large extent’.⁴⁵

(ii) Regulatory competition

A further argument in favour of common EU conflict of laws rules applicable to companies may be seen in the benefits of regulatory competition in company law, insofar as such common rules would broaden the scope of legal questions to be addressed based on the incorporation theory. The obvious parallel would be the United States, where companies can freely choose their state of incorporation and thus the applicable corporate law.⁴⁶ Specifically, this concerns the market for reincorporations: while a mere change in corporate domicile is not possible in the US, the merger of an existing company with a newly-founded shell company in the target state⁴⁷ does not pose significant problems, and in particular does not lead to taxation of hidden reserves.

In the competition between US states, initially New Jersey and later Delaware took front place, in particular as far as listed firms are concerned.⁴⁸ Various reasons have been cited for Delaware’s success.⁴⁹ First, the (re-)incorporation process in Delaware is relatively easy and quick. Second, a specialised and qualified bar and bench promise practice-oriented application of the law and a high degree of legal certainty. Additionally, the influential bar exerts pressure for the continued existence of Delaware’s leading position, since for instance derivative suits in Delaware can be brought only by local lawyers. Third, Delaware itself is dependent on the firms that have only their registered seat here. Delaware receives from them a one-off incorporation fee and a periodic franchise tax. Since this financial advantage has, by contrast with bigger states, a significant effect on the state budget, there is a credible commitment that the law will remain business-friendly. As a result, it may be the case today that Delaware’s position is so dominant that other states do not really compete with it.⁵⁰ Whether Delaware as the main provider of state corporate law in the US is the outcome of a race to the top or one to the bottom is, of course, an age-old question of US corporate law⁵¹.

⁴⁵ Impact Assessment (n 24), 35 and 116.

⁴⁶ See eg § 5.01 Model Business Corporation Act. This goes back to *Paul v. Virginia* 75 U.S. 168 (1868).

⁴⁷ See eg § 252(a) Delaware General Corporation Law.

⁴⁸ For data see Ofer Eldar and Lorenzo Magnolfi, ‘Regulatory Competition and the Market for Corporate Law’ (2020) 12 *American Economic Journal: Microeconomics* 60 (also reporting Nevada’s recent rise).

⁴⁹ See eg Roberta Romano, *The Genius of American Corporate Law* (Washington: AEI Press 1993); Roberta Romano, ‘Market for Corporate Law Redux’ in Francesco Parisi (ed), *Oxford Handbook of Law and Economics* (Oxford: Oxford University Press 2017).

⁵⁰ Lucian A Bebchuk and Assaf Hamdani, ‘Vigorous Race or Leisurely Walk: Re-considering the Competition over Corporate Charters’ (2002) 112 *Yale Law Journal* 553.

⁵¹ William L Cary, ‘Federalism and Corporate Law: Reflections Upon Delaware’ (1974) 83 *Yale Law Journal* 663. This term ‘race to the bottom’ was also used in the Opinion of Advocate General La Pergola in C-212/97 *Centros Ltd v Erhvervsog Selskabsstyrelsen* [1999] ECR I-1459, at 1479 note 48.

In the EU, some may argue that developments of legal capital requirements show that some regulatory competition in company law has taken place already given that private companies from continental Europe had initially incorporated in the UK in order to avoid legal capital requirements which has lead to the abolition or reduction of these requirements in many Member States.⁵² However, there are good reasons to argue that the US debate cannot be simply transferred to the EU context, even if future EU law unequivocally followed the incorporation theory.⁵³ For example, the linguistic, cultural and economic homogeneity of the US states means that shifting the registered seat to another state does not face major informational costs or emotional resistance; yet, this is different in the EU where obstacles such as language barriers cannot be completely removed. As far as competitive pressure exists, it is also doubtful whether European legislators would really compete for ‘the best’ corporate law.⁵⁴ The Member States lack the financial incentives that have influenced Delaware in particular in shaping its law. In the EU, Member States do not generally levy meaningful franchise taxes, and when a company is founded only the administrative costs may be charged.⁵⁵ Nor do other fiscal motives exist, since in general the real seat of a firm is decisive for tax purposes.⁵⁶ Some indirect benefits may be possible, for example, Member States with many foreign incorporations may profit from more clients for lawyers and other consultants, thus collecting more taxes and creating more jobs;⁵⁷ yet, here too, there is no Member State’s where the corporate bar is comparably dependent on winning foreign firms as it is in Delaware.⁵⁸ Finally, it is worth noting that stakeholder interests play a greater role in many European countries which creates special considerations about the risks of regulatory arbitrage.⁵⁹

Overall, the main reason in favour of harmonisation thus remains the need for legal certainty. Regulatory competition can have some benefits as it brings reduced regulatory errors, more innovation and faster learning effects and adaptation responses than with isolated national

⁵² See Martin Gelter, ‘Centros and Defensive Regulatory Competition: Some Thoughts and a Glimpse at the Data’. (2019) 20 *European Business Organization Law Review* 467.

⁵³ See e.g. this see Gerner-Beuerle et al (n 30) (*The Illusion of Motion*), 426.

⁵⁴ Similarly, the assessments by Martin Gelter, ‘The Structure of Regulatory Competition in European Corporate Law’ (2005) 5 *Journal of Corporate Law Studies* 247; Luca Enriques, ‘EC Company Law and the Fears of a European Delaware’ (2004) *European Business Law Review* 1259.

⁵⁵ Enriques, *ibid* at 1271.

⁵⁶ See eg Maisto G Guglielmo (ed). *Residence of Companies Under Tax Treaties and EC Law* (Amsterdam: IBFD 2009).

⁵⁷ See John Armour, ‘Who Should Make Corporate Law? EC Legislation versus Regulatory Competition’ (2005) 58 *Current Legal Problems* 369, 395.

⁵⁸ In addition, it is noticeable that promotion for foreign incorporation in the EU has often been driven by lawyers and other consultants of the real-seat countries, see Marco Becht, Colin Mayer and Hannes Wagner ‘Where Do Firms Incorporate? Deregulation and the Cost of Entry’ (2008) 14 *Journal of Corporate Finance* 241, 255.

⁵⁹ See eg Martin Gelter, ‘Tilting the Balance between Capital and Labor? The Effects of Regulatory Arbitrage in European Corporate Law on Employees’ (2010) 33 *Fordham International Law Journal* 792.

legislation.⁶⁰ Yet, any future EU conflict of laws rules on the law applicable to companies also need to address other interests, such as the legitimate interests of the host countries and third parties (as will be discussed in the following).⁶¹

C. The form of common EU rules

Although the case law of the Court of Justice has had an impact on some core questions of conflict of laws as applicable to companies,⁶² it is clear that it is not feasible to leave it to the Court to design common EU rules in this area of law. The Court does not seek to create a set of common rules of private international law and, on its own, cannot provide sufficient legal certainty in this complex field (e.g., as to the precise scope of the *lex societatis*⁶³).

Another suggestion may be to rely on non-binding common standards that national law-makers may, but do not have to, adopt. This approach could refer to some parallel developments, for example, some of the EU recommendations in the field of corporate governance,⁶⁴ the draft for a European Model Companies Act,⁶⁵ and – as a comparative insight from the United States – the Model Business Corporation Act of the American Bar Association and the Restatement of Conflict of Laws of the American Law Institute.⁶⁶ However, in the present context, such non-binding standards would not be sufficient: due to their voluntary nature, they can only lead to partial convergence. If it is one of the aims of common rules of conflict of laws applicable to companies to provide legal certainty for businesses as they operate across borders, binding uniform rules are needed.⁶⁷

The next question is whether the EU law-maker should pursue the adoption of binding rules in the form of a directive or a regulation. Any consideration of this question has to start with the relevant legal bases. On the one hand, according to Article 50 of the TFEU, harmonisation by means of directives is possible ‘in order to attain freedom of establishment as regards a particular activity’. On the other hand, according to Article 81(1), (2)(c) of the

⁶⁰ See eg Roger Van den Bergh, ‘Towards an Institutional Legal Framework for Regulatory Competition in Europe’ (2000) 53 *Kyklos* 435, 437–8; Harald Baum, ‘Globalization Capital Markets and Possible Regulatory Responses’ in Jürgen Basedow and Toshiyuki Kono (eds), *Legal Aspects of Globalization* (The Hague: Kluwer Law International 2000), 77, 104–5.

⁶¹ See Section IV.B, below.

⁶² See Section II.B, above.

⁶³ Discussed further in Section IV.B, below.

⁶⁴ Eg Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board (2005/162/EC).

⁶⁵ See <http://law.au.dk/en/research/projects/european-model-company-act-emca/>.

⁶⁶ See https://www.americanbar.org/groups/business_law/committees/corplaws/ and <https://www.ali.org/publications/show/conflict-laws/>

⁶⁷ For a similar point see Thomas S Ulen, ‘Economic and Public-Choice Forces in Federalism’ (1997/98) 6 *George Mason Law Review* 921, 928 (‘If the costs and benefits of an action, whether public or private, stray across jurisdictional lines, then the highest level of government that can fully internalize the costs and benefits of the action ought to take responsibility’).

TFEU, the EU can, for the purpose of ‘judicial cooperation in civil matters having cross-border implications (...) adopt measures, particularly when necessary for the proper functioning of the internal market, aimed at ensuring (...) the compatibility of the rules applicable in the Member States concerning conflict of laws and of jurisdiction’.

We submit that it is preferable to harmonise conflict of laws rules by means of a ‘Rome V Regulation for the Harmonisation of the Law Applicable to Companies’. This approach is in line with the existing ‘Rome regulations’ on other matters of private international law.⁶⁸ Regulations also have the advantage of creating EU-wide conceptual uniformity, since all Member States and their courts will apply and interpret the same legal definitions and rules. While there can be instances where topics should be left to the discretion of the Member States, this does not mean that a regulation is unsuitable. Rather, as with other regulations,⁶⁹ it is possible to explicitly provide that certain well-defined issues can be left to the Member States, for example, in order to protect local interests.⁷⁰

In the long term, it would be helpful if a new regulation on conflict of laws rules applicable to companies and all existing (and future) ‘Rome regulations’ were merged into one regulation. Such a consolidated regulation (‘European Code of Private International Law’)⁷¹ could clarify ambiguities about the relationship between the *lex societatis*, the *lex contractus*, the *lex loci delicti* etc. and may therefore foster the ‘unity of the legal order’.⁷² It could also address some of the common themes of private international law (*ordre public*, *renvoi* etc).

D. Preliminary conclusion

The reasoning presented in this section suggests that EU harmonisation of the conflict of laws rules applicable to companies can have substantive benefits. While empirical legal research is often uncertain about the positive effects of legal reform,⁷³ it is likely that such unified

⁶⁸ See note 4, above.

⁶⁹ Eg, Council Regulation 2157/2001 on the Statute for a European company (SE) [2001] O.J. L294/1.

⁷⁰ See also Section IV.B, below, in particular for the topic of employee participation in sub-section (iv).

⁷¹ For previous suggestions see Giesela Rühl and Jan von Hein, ‘Towards a European Code on Private International Law?’ (2015) 79 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 701; Xandra E Kramer, ‘Current Gaps and Future Perspectives in European Private International Law: Towards a Code on Private International Law?’ (Briefing Note, PE 462.476, European Parliament, 2012); Marcin Czepelak, ‘Would we like to have a European Code of Private International Law?’ (2010) *European Review of Private Law* 705; Mathias Siems, ‘Führen alle Wege aus dem Dschungel nach Rom? - Möglichkeiten und Grenzen der Vereinheitlichung des internationalen Privatrechts’ (2003/2004) *Zeitschrift für Gemeinschaftsprivatrecht* (GPR) 66 (‘Europäisches Gesetzbuch für internationales Privatrecht’).

⁷² See eg Manfred Baldus, *Die Einheit der Rechtsordnung: Bedeutungen einer juristischen Formel in Rechtstheorie, Zivil- und Staatsrechtswissenschaft des 19. und 20. Jahrhunderts* (Berlin: Duncker & Humblot 1995). But see also Andreas Fischer-Lescano and Gunther Teubner, ‘Regime-Collisions: The Vain Search for Legal Unity in the Fragmentation of Global Law’ (2004) 25 *Michigan Journal of International Law* 999.

⁷³ For some of the problems see Christoph Engel, ‘Empirical Methods for the Law’ (2018) 174 *Journal of Institutional and Theoretical Economics* 5; Holger Spamann, ‘Empirical Comparative Law’ (2015) 11 *Annual Review of Law and Social Science* 131.

conflict rules can indeed address existing problems of legal uncertainty in this field. Still, at this point, our conclusion needs to be a preliminary one, since harmonised rules need to be well-designed, notably in terms of choosing ‘the right’ connecting factor based on the incorporation or real seat theory.⁷⁴ Thus, the next section will discuss how far it is possible – and potentially beneficial – to design such rules.

IV. Possible harmonisation based on the ‘incorporation theory’

A. Critical analysis of proposals for an EU-wide incorporation theory

Some Member States have codified, at least to some extent, the conflict of laws rules applicable to companies, namely: Belgium, Bulgaria, Czech Republic, Estonia, Italy, Lithuania, Netherlands, Poland, Portugal, Romania, and Spain.⁷⁵ In addition, a number of private and public bodies have submitted proposals for a codification of private international company law in the EU or even wider afield: these are the private proposals by the European Group for Private International Law (GEDIP) from 2015,⁷⁶ the ‘Sonnenberger Group’ from 2007,⁷⁷ and the Institute of International Law from 1965,⁷⁸ as well as an EC Convention from 1968⁷⁹ and a Hague Convention from 1956,⁸⁰ which have both never entered into force.

Most of these texts favour a connecting factor that is based on some form of the incorporation theory, understood in a broad sense. This is the case with both the GEDIP and Sonnenberger proposals, which stipulate that companies shall be governed ‘by the law of the country under which [they have] been incorporated’ (or, as far as unincorporated entities are concerned, by the law under which they have been formed)⁸¹ and by ‘the law of the state in whose public register they are entered’,⁸² respectively.⁸³ Legislators and/or national courts in most Member States also seem to be of the opinion that the real seat theory is no longer an available policy

⁷⁴ See Section II.A, above.

⁷⁵ For details see Gerner-Beuerle et al (n 29), 10–1.

⁷⁶ GEDIP, ‘Draft rules on the law applicable to companies and other bodies’ (2016), available at <https://www.gedip-egpil.eu/documents/Milan%202016/GEDIPs%20Proposal%20on%20Companies.pdf>.

⁷⁷ Hans Jürgen Sonnenberger (ed.), *Vorschläge und Berichte zur Reform des europäischen und deutschen internationalen Gesellschaftsrechts* (Tübingen: Mohr Siebeck 2007) (proposal by the German expert group on private international law).

⁷⁸ The Institute of International Law, ‘Companies in Private International Law’ (1965), available at https://www.idi-iil.org/app/uploads/2017/06/1965_var_02_en.pdf.

⁷⁹ EC Convention on the Mutual Recognition of Companies and Bodies Corporate of 29 February 1968, Bulletin of the European Communities, Supplement 2/69, 7-18.

⁸⁰ Hague Convention concerning the recognition of the legal personality of foreign companies, associations and institutions 1956, available at <https://www.hcch.net/en/instruments/conventions/full-text/?cid=36>.

⁸¹ GEDIP proposal, Art. 3.

⁸² Sonnenberger proposal, Art. 2(1).

⁸³ See also Art 1 of the EC Convention 1968 (n 79), which referred to the ‘statutory seat’ to much the same effect.

choice with respect to EU-incorporated companies in light of the decisions of the Court of Justice in *Centros*, *Überseering* and *Inspire Art.*⁸⁴

Indeed, there are at least two reasons that support such an approach. First, legal certainty may militate in favour of a form of incorporation theory. Member States differ in their definitions of the real seat, and past experience with a real-seat-type connecting factor used by the Insolvency Regulation (the ‘centre of main interest’, COMI) shows that such a connecting factor is likely to give rise to a considerable amount of litigation and, accordingly, a high degree of legal uncertainty.⁸⁵ Second, EU law-making needs to consider the expectations of the various constituencies involved and the desirability of a system of more or less extensive corporate mobility. Most of the Member States *de facto* use the place of incorporation or registered seat as the main or exclusive connecting factor in relation to companies from other Member States.⁸⁶ Thus, mandating a connecting factor other than the registered office (or any other version of the incorporation theory) would likely give rise to significant transitioning costs. In addition, mandating a uniform connecting factor inspired by the real seat theory in a future Rome V Regulation would significantly reduce corporate mobility and the possibility for undertakings to choose the company law rules that best fit their needs; such a choice might thus be seen as conflicting with the aims of the Treaty as interpreted by the Court of Justice, at least regarding rules and principles regulating companies’ internal affairs.⁸⁷

Thus, a company should be governed by the law according to which it has been incorporated, and an unincorporated entity by the law according to which it has been formed. Given the differences in Member State laws, it may prove useful to include a definition of ‘incorporated companies’ as all companies that acquire legal personality upon entry in the commercial or companies register of the jurisdiction of formation. This may increase legal certainty in relation to some partnerships and related business organisations in a number of Member States.⁸⁸ While such a rule should capture most cases, it may be useful to supplement the provision with a ‘residual clause’ similar to the one contained in the GEDIP proposal to the effect that the law of the closest connection shall apply if the law cannot be determined pursuant to the general rule.⁸⁹ The residual clause may, for example, apply to cases where founders from more than one country draw up an instrument establishing a company in a common language without specifying explicitly the governing law and where registration of the company/partnership is not required or where such registration has merely a declaratory

⁸⁴ See Section II.A, above, as well as Gerner-Beuerle et al (n 29), 195–206.

⁸⁵ See eg Wolf-Georg Ringe, ‘Forum Shopping under the EU Insolvency Regulation’ (2008) 9 *European Business Organization Law Review* 579.

⁸⁶ For details see Gerner-Beuerle et al (n 29), 24–31, 40–4. But see also Table 1 in Section III.A, above (Poland and Portugal being the main exceptions).

⁸⁷ See also Gerner-Beuerle and Schuster (n 34), 329 (strict real seat approach would be incompatible with the Treaty as interpreted by the Court of Justice in *Überseering*).

⁸⁸ The legal nature of partnerships differs across countries; see, eg, Mathias Siems, ‘Regulatory Competition in Partnership Law’ (2009) 58 *International & Comparative Law Quarterly* 767.

⁸⁹ GEDIP proposal, Art. 4.

effect. In order to ensure legal certainty, this clause should not be formulated as a general escape clause comparable to the one applicable to international torts in the Rome II Regulation⁹⁰ or in the Slovenian Private International Law and Procedure Act.⁹¹ Rather, it should be made clear that it has a residual function that is only engaged if the determination of the incorporation or formation law fails.

The alternative to the solution proposed here would be the adoption of an EU-wide real seat theory. The ‘real seat theory’ addresses the risks that arise as a result of the divergence between the country that promulgates the applicable rules of company law and the country where the most-affected interests are situated. This situation is particularly troublesome when the most-affected country protects local interests also through company law rules. Such local rules would be circumvented through the application of a foreign company law, which may produce ‘negative externalities’ for certain stakeholders if these are less well protected under the applicable law. Additionally, another argument in favour of the ‘real seat theory’ (in any of its forms) may be that the connecting factor for company law needs to be integrated into the existing body of national and European private international law. Insolvency law in particular does not use the connecting factor of the place of incorporation, but the centre of main interest (COMI) to determine the applicable insolvency law.⁹² As the COMI is more akin to the connecting factor under the real seat theory, an EU-wide real seat theory could have advantages in that friction with insolvency law would be avoided.

Another possible solution is to accept that connecting factors operate differently in different areas of the law, but clarify precisely how these areas are to be defined – also with the effect that it would be more difficult for Member States to shift legal solutions from one area of law to another in order to change the connecting factor.⁹³ A possible model could be the US approach, which narrowly limits the scope of company law to the internal affairs of the company.⁹⁴ The recent judgments by the Court of Justice in *Kerr* and *Verein für Konsumenteninformation* seem to point in a similar direction as they state that the reference in the Rome I Regulation to questions governed by the law of companies⁹⁵ exclusively applies ‘to the

⁹⁰ Regulation (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (Rome II), Art. 4(3) [in the following: Rome II Regulation].

⁹¹ Art. 2 of the Slovenian Private International Law and Procedure Act 1999 (English translation available at https://arbitrationlaw.com/sites/default/files/free_pdfs/Slovenia%20PILPA.pdf).

⁹² See Section IV.B, below.

⁹³ As happened in insolvency law, see B(ii), below.

⁹⁴ See American Law Institute, *Restatement of the Law, Conflict of Law* (2nd edn, St. Paul, Minn.: American Law Institute, 1971): § 296: ‘In order to incorporate validly, a business corporation must comply with the requirements of the state in which incorporation occurs regardless of where its activities are to take place or where its directors, officers or shareholders are domiciled’; § 297: ‘Incorporation by one state will be recognized by other states.’ For an overview see Christian Kersting, ‘Corporate Choice of Law – A Comparison of the United States and European Systems and a Proposal for a European Directive’ (2002-2003) 28 *Brooklyn Journal of International Law* 7; Federico M Mucciarelli, ‘The Function of Corporate Law and the Effects of Reincorporations in the U.S. and the EU’ (2012) 20 *Tulane Journal of International and Comparative Law* 449.

⁹⁵ Art. 1(2)(f) Rome I Regulation.

structural aspects' of companies.⁹⁶ Such a solution would possibly reduce negative externalities that may arise from the application of a company law that is different from the law protecting local stakeholders. However, the company laws of the EU Member States vary more widely than their US counterparts. Thus, it is questionable whether simply adopting the US internal affairs doctrine would be sufficient. Consequently, we suggest that an EU-wide rule needs to consider the boundary issues with other areas of law and the content of national law more closely, as discussed in the following section.

B. Delimiting the scope of company law

(i) General considerations

Most existing conflict of laws rules for companies, both in Member States that have codified the rules and in proposals on a harmonisation of private international law, provide for a non-exhaustive enumeration of topics that shall be governed by the *lex societatis*. The questions covered by the *lex societatis* are generally relatively uncontroversial, and a comparative analysis of the EU Member States finds far-reaching consensus on the topics to be included in such a list (as will be shown here). A recent opinion by Advocate General Saugmandsgaard Øe in *Verein für Konsumenteninformation* also expresses the view that, in order to identify what constitutes a question governed by the law of companies, a 'case-by-case approach must be adopted, looking to the general principles which stem from the corpus of the national legal systems'.⁹⁷

⁹⁶ C-25/18 *Brian Andrew Kerr v Pavlo Postnov and Natalia Postnova* ECLI:EU:C:2019:376, para 33; C-272/18 *Verein für Konsumenteninformation v TVP Treuhand- und Verwaltungsgesellschaft für Publikumsfonds mbH & Co KG* ECLI:EU:C:2019:827, para 35.

⁹⁷ Opinion of Advocate General Saugmandsgaard Øe, delivered on 5 September 2019, C-272/18 *Verein für Konsumenteninformation v TVP Treuhand- und Verwaltungsgesellschaft für Publikumsfonds mbH & Co KG* at para 47 citing Gerner-Beuerle et al (n 29).

Table 2: Subjects mentioned explicitly as falling in the scope of the lex societatis⁹⁸

Topic	BE	BG	CZ	EE	IT	LT	NL	PL	PT	RO	ES	G ⁹⁹	S ¹⁰⁰	DE ¹⁰¹
1. Formation and legal nature/personality	yes	yes	yes											
2. Corporate Name	yes	yes	yes	yes	yes	yes	no	yes	no	no	no	yes	yes	yes
3. Capacity of company and authority of organs	yes	yes	yes											
4. Capital structure	no	yes	yes	yes										
5. Rights and obligations of members	yes	yes	yes	yes	yes	no	no	yes	yes	yes	no	yes	yes	yes
6. Internal management matters (corporate governance structure)	yes	yes	yes											
7. Duties of directors and liability for a breach of duty	yes	yes	no	no	yes	yes	yes	yes	no	no	no	yes	yes	yes
8. Liability of shareholders for the debts of the company	no	yes	yes	yes	yes	yes	no	yes	yes	yes	no	yes	yes	yes
9. Voluntary winding up	yes	yes	yes											
10. Derivative action and other enforcement issues	no	no	no											
11. Group law	no	no	no											
12. Financial reporting, audits	no	yes	yes	no										

In order to facilitate a comparison and the identification of a common denominator, Table 2 gives an overview of the topics that are explicitly mentioned as falling within the scope of the applicable law pursuant to the laws of different Member States that contain an enumeration of such matters and the policy initiatives mentioned above.¹⁰² It should be emphasised that this

⁹⁸ Unless otherwise noted, abbreviations refer to the Member States' two-letter ISO code.

⁹⁹ GEDIP proposal (n 76).

¹⁰⁰ Sonnenberger proposal (n 77).

¹⁰¹ The German rules are from a draft legislation from 2008 that was not adopted, Referentenentwurf, 'Gesetz zum Internationalen Privatrecht der Gesellschaften, Vereine und juristischen Personen', available at http://www.gesmat.bundesgerichtshof.de/gesetzesmaterialien/16_wp/int_gesr/int_gesr-index.htm.

¹⁰² Note that this table simplifies the very complex underlying questions. Just as the exact definition of the scope of the *lex societatis* differs across Member States, so does the definition of the topics included in this table.

Table refers only to matters that are expressly enumerated in the relevant legislation. Many relevant issues, notably a company's capacity and legal nature, formation and dissolution, capital structure, internal governance matters, the acquisition and loss of the status as a shareholder or member, as well as the ensuing rights and duties of shareholders, directors' duties, and the liability of directors *to the company* for a breach of duties, concern core issues of company law. As far as can be seen, it is not contested that these questions should be governed by the *lex societatis* even where any explicit reference to them is omitted in the relevant codifications of the Member States. Two contentious issues are the liability of directors for conduct that may cause a loss not only to the company, but also or exclusively *to third parties*, and the liability of shareholders for the obligations of the company ('piercing the corporate veil'), which is assigned to the *lex societatis* in the majority of Member State codifications and also treated as falling under the *lex societatis* in some of the Member States without a codified private international law.¹⁰³

With regard to items 1 to 7 and 9 of Table 2, a non-exhaustive enumeration in harmonised law would reflect a wide consensus in the Member States. Therefore, we propose that a future Rome V Regulation should include an enumeration of these matters in order to give guidance as to the autonomous interpretation of the scope of the *lex societatis*. In addition, the regulation should make it clear that the enumeration is non-exhaustive, since no list can anticipate all relevant questions of delimitation and it is consequently essential to retain flexibility to develop the law further. This would also be in line with the approach in other relevant legislative measures at the European level, for example the Insolvency Regulation.¹⁰⁴

To be sure, a comparative solution based on the existing rules of the Member States does not always provide clear or suitable answers. Thus, it is also necessary to develop some general principle (or a set of principles) that can determine whether or not a particular belongs to the *lex societatis*. We suggest that the most general principle is that there are legal questions where the legitimate interests of the host country both outweigh legal certainty arguments and general benefits choice of law, and where – absent harmonisation – the host country would likely be able to successfully justify under *Gebhard* an application of its own company law to a foreign-registered company. The precise justification for these legitimate interests can vary according to the issues at stake. Often, it will be the case that it concerns the need to protect third parties that are not able to protect themselves.¹⁰⁵ However, it is also clear that *any* company law will ultimately reflect a particular trade-off between interests of various stakeholders, such as shareholders, creditors and (often) employees. Thus, the requirement of legitimate interests goes beyond the mere fact that a stakeholder has a connection to another

¹⁰³ For the latter point see eg Lord Collins in *Dicey, Morris & Collins on the Conflict of Laws* (15th edn, London Sweet & Maxwell 2012), para 30-028.

¹⁰⁴ As discussed in the following sub-section (ii) below.

¹⁰⁵ In the terminology of regulatory competition, see Section III.B.(ii), above, this may therefore be understood as a form of 'market failure'.

country. Finally, a future Rome V Regulation needs to consider that it aims to harmonise a residual regulatory space. Thus, as far as there already EU conflict of laws rules that address certain areas of law (notably, insolvency law and tort law, as discussed in the following sections), it needs to both respect their decisions about connecting factors different from the *lex societatis* and to produce regulatory outcomes consistent with them.

A simple example of applying this principle is the name under which the company trades. While the choice of the name is widely regarded as falling within the scope of the *lex societatis* (see item 2 of Table 2), it also touches upon important policy interests of the host state. The relevant problems often arise only in the context of a company's cross-border activity. For instance, a corporate name may not be misleading or give rise to a risk of confusion in the Member State of incorporation, but may well do so in the host state. Policy makers and commentators in a number of Member States are therefore of the opinion that certain regulatory requirements of the host state may effectively override the *lex societatis* in order to protect third parties transacting with the company in the host state.¹⁰⁶

The following sub-sections will deal with three more complex and contentious situations in which questions about the limits of the scope of the *lex societatis* are at stake: the relationship to insolvency law, directors' liability under tort law, and employee co-determination.

(ii) *Lex societatis and lex concursus*

In EU law, the question of whether to classify rules as falling within the *lex societatis* or the *lex concursus* has so far largely been shaped by the Insolvency Regulation.¹⁰⁷ The Regulation provides that the *lex concursus* shall determine the conditions for the opening of insolvency proceedings, their conduct and closure, and further lists a number of questions falling within the scope of international insolvency law.¹⁰⁸ Most of these questions are concerned with the operation and effects of the insolvency proceedings themselves. They fall clearly outside of the *lex societatis* and problems of demarcation are unlikely to arise with regard to them. Nevertheless, the exact boundaries of the *lex concursus* are difficult to draw because the Court of Justice has held that the courts that have jurisdiction to open insolvency proceedings (the courts of the Member State where the company's COMI is located¹⁰⁹) also have

¹⁰⁶ For details see Gerner-Beuerle et al (n 29), 66–79 (column on ‘company name’).

¹⁰⁷ Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings, OJ L141/19 (Insolvency Regulation Recast) (formerly Regulation (EC) No 1346/2000). See also Federico M Mucciarelli, ‘Private International Law Rules in the Insolvency Regulation Recast: A Reform or a Restatement of the Status Quo?’ (2016) 13 *European Company and Financial Law Review* 1; Reinhard Bork and Renato Mangano, *European Cross-Border Insolvency Law* (Oxford: Oxford University Press 2016) 106–116.

¹⁰⁸ Regulation (EU) 2015/848, Art. 7(2)

¹⁰⁹ Regulation (EU) 2015/848, Art. 3(1).

jurisdiction to hear ‘actions which derive directly from [insolvency] proceedings and which are closely connected to them’.¹¹⁰

The Court’s case law has now been codified in the Insolvency Regulation Recast, which mentions avoidance actions as an example of such closely connected actions.¹¹¹ However, the Regulation does not provide for any definition of closely connected actions, but merely summarises some of the Court of Justice case law in the recitals.¹¹² Thus, two questions arise that are of importance in the present context: first, how closely connected actions are to be defined in general terms, and second, whether the definition thus derived is only relevant for the determination of the jurisdiction of the court of the insolvency proceedings, or whether jurisdiction and the applicable law go hand in hand and closely connected actions, accordingly, are always governed by the *lex fori*.

In its case law, the Court of Justice made a number of important points that can guide the development of a general definition of closely connected actions. First, the Court has pointed out that the scope of Article 3(1) of the Insolvency Regulation Recast (international jurisdiction) and the bankruptcy exception of the Judgments Regulation¹¹³ are mutually exclusive and exhaustive.¹¹⁴ Given that the legislator intended the Judgments Regulation to have a broad scope of application, encompassing all civil and commercial matters except certain well-defined issues,¹¹⁵ it follows that the scope of the Insolvency Regulation is to be interpreted narrowly.¹¹⁶ Second, ‘the decisive criterion’ to distinguish between civil and commercial matters and actions that derive from insolvency law ‘is not the procedural context of which that action is part, but [its] legal basis’.¹¹⁷ Thus, the Court asks ‘whether the right or the obligation which [constitutes] the basis of the action finds its source in the common rules of civil and commercial law or in the *derogating rules* specific to insolvency proceedings.’¹¹⁸ In addition, in several decisions, the Court stressed that the purpose of the action was the protection of the interests of ‘the general body of creditors’¹¹⁹ and that the

¹¹⁰ C-339/07 *Christopher Seagon v Deko Marty Belgium NV* [2009] ECR I-767, para 21 (dealing with avoidance actions).

¹¹¹ Regulation (EU) 2015/848, Art. 6(1).

¹¹² Recital 35 of Regulation (EU) 2015/848.

¹¹³ Now Art. 1(2)(b) of Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Recast Brussels Regulation).

¹¹⁴ The two provisions ‘must be interpreted in such a way as to avoid any overlap between the rules of law that those texts lay down and any legal vacuum’, C-157/13 *Nickel & Goeldner Spedition GmbH v ‘Kintra’ UAB*, ECLI:EU:C:2014:2145, para 21.

¹¹⁵ Regulation (EU) No 1215/2012, recital 10.

¹¹⁶ C-292/08 *German Graphics Graphische Maschinen GmbH v Alice van der Schee* [2009] ECR I-8421, para 25.

¹¹⁷ *Nickel & Goeldner* (n 114), para 27.

¹¹⁸ Ibid. (our emphasis). Similar Case 133/78 *Gourdain v Nadler* [1979] ECR 733, para 5.

¹¹⁹ *Gourdain v Nadler*, ibid.; *Seagon v Deko Marty* (n 110), para 16; C-213/10 *F-Tex SIA v Lietuvos-Anglijos UAB ‘Jadecloud-Vilma’*, ECLI:EU:C:2012:215, para 32; C-147/12, *ÖFAB v Frank Koot*, ECLI:EU:C:2013:490, para 25.

action was ‘the exclusive prerogative of the liquidator’,¹²⁰ which was ‘brought in the context of insolvency proceedings’.¹²¹ On the other hand, if the action *could* also be brought by the liquidator, but it was actually ‘brought outside the context of insolvency proceedings [it] may fall within the scope of ... Regulation No 44/2001.’¹²² Summarising this case law, it can accordingly be said that the concept of ‘closely connected action’ is based on three criteria. Closely connected actions (i) derogate from common rules of civil and commercial law; (ii) are adopted in the interests of the general body of creditors; and (iii) are in fact brought by the liquidator in the context of insolvency proceedings, rather than by individual creditors.

Whether these criteria can be transposed to the question of the applicable law has been addressed by the Court in the decision *Kornhaas*.¹²³ In this case, dealing with the classification of a provision of German law imposing liability on managers of a private limited company for payments made after cash-flow insolvency or over-indebtedness,¹²⁴ the Court held that the German liability provision fell within the scope of the applicable law as set out in the Insolvency Regulation. By interpreting what is now Article 7(2) Insolvency Regulation Recast, the Court stressed that ‘the conditions for the opening of [insolvency] proceedings’ within the meaning of that provision included ‘the consequences of an infringement of [the] obligation’ to apply for the opening of proceedings.¹²⁵ However, the Court’s decision is, arguably, more sweeping. The Court went beyond the codified scope of the *lex concursus* by embracing explicitly its case law concerning jurisdiction, especially its judgment in *H v H.K.*,¹²⁶ which dealt with the same provision of German law. Given that the liability provision was to be qualified as a closely connected action, as decided in *H v H.K.*, the Court held that it ‘must be regarded as being covered by the law applicable to insolvency proceedings and their effects’.¹²⁷ Thus, it seems highly likely that the three criteria outlined above are intended to apply similarly to the determination of the scope of the *lex concursus*.

However, relying on these criteria entails the problem that the classification of legal mechanisms at the intersection of company law and insolvency law depends on technical, and functionally not necessarily justified, differences in the formulation of the internal law. In particular, the necessary involvement of a liquidator may depend on relatively arbitrary idiosyncrasies of the national law. According to this criterion, some liability provisions, for

¹²⁰ *ÖFAB v Frank Koot*, ibid.

¹²¹ C-295/13 *H v H.K.*, ECLI:EU:2014:2410, para 20.

¹²² Ibid. para 25.

¹²³ C-594/14 *Simona Kornhaas v Thomas Dithmar*, ECLI:EU:C:2015:806.

¹²⁴ Now s. 64, sentence 1 German Limited Liability Companies Act (GmbHG). The reference was made by BGH, decision of 2 Dec. 2014, II ZR 119/14.

¹²⁵ *Kornhaas* (n 123), para 19.

¹²⁶ See above note 121.

¹²⁷ *Kornhaas* (n 123), para 17.

example wrongful trading pursuant to English law¹²⁸ and the French *action en responsabilité pour insuffisance d'actif* (liability for insufficiency of assets),¹²⁹ would be classified as insolvency law for purposes of private international law. The same would hold for the liability of company directors for the failure to file for the opening of insolvency proceedings under German law, as far as the loss suffered by pre-duty creditors was concerned (creditors whose claims existed at the time when the duty to file arose),¹³⁰ but not as regards the loss suffered by post-duty creditors, because the latter have standing to sue individually even if insolvency proceedings are opened.¹³¹ Likewise, in the Czech Republic, directors can be held liable for the debts of a company if they knew, or should have known, that the company was facing an imminent threat of bankruptcy and, in breach of the duty of care, failed to take all necessary steps to prevent the bankruptcy. Again, creditors have standing to bring a lawsuit in separate proceedings independent of any decision by the insolvency court.¹³²

An additional problem is the potential misalignment of legal mechanisms from insolvency law and company law. Since it is proposed to base a future Rome V Regulation on the incorporation theory, insolvency law and company law would use two different connecting factors. This may give rise to the risk of regulatory gaps or the cumulative application of legal mechanisms from different jurisdictions, leading to potential over-deterrance. This problem exists, first of all, if the demarcation between the *lex societatis* and the *lex concursus* is not well established; this is currently the case in many, if not most, Member States.¹³³ In this case, the risk exists that the COMI Member State classifies a legal mechanism as company law for purposes of private international law and the state of incorporation as insolvency law, thus leading to a negative conflict of the applicable law, or vice versa, leading to a positive conflict. This situation is likely to continue to exist for some time as the Court of Justice slowly establishes the demarcation from the viewpoint of the Insolvency Regulation. However, the problem may persist even after well-established criteria to delimit the *lex societatis* and the *lex concursus* have been developed by policy makers or courts. Member States may utilise legal mechanisms of differing design and provenance to address the same social conflict. While conflicts that arise in insolvency and in the vicinity of insolvency will be governed by a combination of company law and insolvency law in most Member States, jurisdictions may place different emphasis on one strategy or the other. If a legal system that may provide for an adequate regulatory environment if applied as a whole is

¹²⁸ Section 214 UK Insolvency Act 1986; for the classification of wrongful trading see *Oakley v Ultra Vehicle Design Ltd* [2006] BCC 57, para 42.

¹²⁹ Art L.651-2 of the French Commercial Code. For the classification see *Gourdain v Nadler* (n 118).

¹³⁰ Such creditors are limited to recovering the loss suffered because of the delay in filing, i.e. the difference between the recovery rate that they could have obtained in the case of timely filing and the actual rate (so-called ‘rate reduction loss’ or *Quotenschaden*).

¹³¹ BGHZ 126, 181, 201.

¹³² Section 68 of the Business Corporations Act. For a discussion of the provision see also the Czech country report by Monika Pauknerová and Jan Brodek in Gerner-Beuerle et al (n 29), 321–2.

¹³³ These problems of legal uncertainty have also been identified in the empirical survey of the initial report, see Gerner-Beuerle et al (n 28), 65–99.

dissected as a result of the use of different connecting factors, the same negative and positive conflicts may occur that were described above.¹³⁴

A straight-forward solution to this problem would be the use of the same connecting factor for legal areas as closely related as company law and insolvency law. However, it is unlikely that the connecting factor of the Insolvency Regulation will be amended in connection with the enactment of a possible future Rome V Regulation. In addition, the use of the incorporation law as the *lex societatis* and the law at the COMI as the *lex concursus* can be rationalised in light of the different interests that are typically at play in the two areas, with choice of law being generally less desirable in insolvency law than in company law.¹³⁵ In any case, for most purposes, the problem of positive and negative conflicts in the applicable law can be mitigated by providing in a future Rome V Regulation that legal mechanisms designed to address problems arising specifically in insolvency or in the vicinity of insolvency shall not be included in the scope of the *lex societatis*.

Thus, we suggest that the definition of the scope of the *lex societatis* should include a ‘functional carve-out’ following the general principle (discussed in (i), above) that a future Rome V Regulation needs to accept the rules of conflict of laws applicable in other areas of law and given that legitimate interests of the host country can, in the present case, justify the use of the *lex concursus*. Of course, correctly understood, the scope of both the *lex societatis* and the *lex concursus* are to be determined functionally, i.e. they should be differentiated by taking account of the function of the legal mechanism as addressing conflicts between the relevant corporate actors while the company is a going concern and when it is, or is about to become, insolvent, respectively. In this sense, the functional carve-out is merely declaratory. However, relying on a classification along purely functional lines may, in itself, create legal uncertainty, as many core company law rules also serve the purpose of, for instance, reducing the risk of insolvency.¹³⁶

An explicit carve-out combined with an enumeration of matters falling within the scope of the *lex societatis* would thus serve an important function, not least because the solution suggested here would also mean a partial deviation from the criteria the Court of Justice has developed to define closely connected actions. Specifically, a functional determination of the boundary region between company law and insolvency law would characterise all mechanisms designed to mitigate risk-shifting in the vicinity of insolvency as insolvency law, irrespective of the internal classification of the provision in the Member State’s company or insolvency law. If defined in this way, the first and second criteria used by the Court to determine whether an action is ‘closely connected’ (derogation from common rules of civil

¹³⁴ Gerner-Beuerle and Schuster (n 34), 323–8.

¹³⁵ See eg the discussion in Federico M Mucciarelli, ‘Not Just Efficiency: Insolvency Law in the EU and Its Political Dimension’ (2013) 14 *European Business Organization Law Review* 175.

¹³⁶ One could even argue, for instance, that minimum capital rules fall into this category.

and commercial law, and protection of the interests of the general body of creditors) would retain their significance. However, the third, rather formalistic criterion (involvement of the liquidator in insolvency proceedings) would not be applicable. This is indeed the criterion that, as argued here, leads to results that depend often on idiosyncrasies of the national law and that are difficult to substantiate on functional grounds.

Even under the solution suggested here, differences in the internal laws of the Member States¹³⁷ would not become entirely irrelevant. We suggest that a legal mechanism would be characterised as company law for purposes of private international law if it regulates the structure and operation of the company as a going concern, starting with the company's formation, and independently of the company's financial position. Conversely, it would be characterised as insolvency law if it derogated from the common rules of civil and commercial law and applied only from a certain 'trigger point' onwards that was defined with reference to the company's financial situation. The formulation of the trigger point would necessarily vary to some degree between the Member States, since the respective rules of company and insolvency law that apply in the vicinity of insolvency are not harmonised by either the Company Law Directives or the Insolvency Regulation. Save future legislative action by the EU institutions, these differences in determining when the body of rules designed to address the problem of risk-shifting in the vicinity of insolvency is triggered would need to be respected by the conflict rules embedded in the Insolvency Regulation and the Rome V Regulation. The autonomous concept of 'connected action' builds on the trigger point pursuant to national law,¹³⁸ but it does not determine the trigger point itself, since it is a jurisdictional and conflicts rule. This is also in line with the general principle that legitimate interests of the host country can deviate from the *lex societatis*; in other words, in the present case, the choice of the right trigger point aims at protecting creditors from risks arising from a company's insolvency and can therefore be characterised as *lex concursus*, governed by the Member State of the debtor's COMI.

On the other hand, a conflicts rule that delineates company law and insolvency law on the basis of the function of the mechanism of substantive (internal) law as addressing risk shifting from shareholders to creditors that occurs specifically in financial distress (since financial distress leads to incentive misalignments that do not exist otherwise¹³⁹) allows the Court of Justice to ensure a certain EU-wide consistency in the classification of the relevant

¹³⁷ Only some aspects of insolvency procedures have been harmonised in the EU by Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency).

¹³⁸ Both under the functional approach suggested here and under the current test of the Court of Justice, because 'provisions derogating from the general rules of civil law' (*Nickel & Goeldner* (n 114), para 24) will become operational when the trigger point is reached.,

¹³⁹ Shareholders may take decisions that do not have a net present value and hence do not maximise the overall market value of the firm, see Gerner-Beuerle and Schuster (n 34), 301.

legal mechanisms.. The Court of Justice will be able to review, as part of the interpretation of the conflicts rule suggested here, whether the mechanism of substantive law is triggered by a condition that falls within the range of what can plausibly be claimed to be an approximation of the point where such risk shifting occurs. If it is not, the mechanism does not come within the scope of the insolvency conflicts rule.

In summary, the following mechanisms, whose classification is at present controversial, would clearly be governed by the *lex concursus*: the duty to file and liability for failure to file (notwithstanding whether the claim is brought by the liquidator or, as in the case of liability to post-duty creditors pursuant to German law), wrongful trading, *responsabilité pour insufisance d'actif*, and also — in contrast to what is probably currently the prevailing opinion — the shift of directors' duties that occurs in some legal systems in the vicinity of insolvency.¹⁴⁰

(iii) Liability of directors for non-contractual obligations

As far as the liability of company directors is concerned, Member States largely follow one of three approaches in determining the boundary between the *lex societatis* and the *lex loci delicti*,¹⁴¹ which may inform the determination of boundary conditions in a possible future Rome V Regulation. Under the first approach, the distinction is drawn along the lines of substantive law. Liability questions that arise from a breach of directors' duties, the articles of association, or more generally from a breach of company law, are characterised as company law for purposes of private international law, and situations where liability arises from a wrongful act that is not grounded in company law – and that does not consist in the breach of contract or trust either – are characterised as a non-contractual obligation, and hence be made subject to the Rome II Regulation.¹⁴² Second, a conflict rule can distinguish according to the type of injured party: the *lex societatis* governs any mechanism that gives rise to liability if the loss is caused to the company (and only so-called reflective loss to the shareholders), and the *lex loci delicti* governs damages claims of third parties that suffer a direct (i.e. not only reflective¹⁴³) loss. Finally, according to the third approach, the distinction is based on the type

¹⁴⁰ For the latter point see the overview in Gerner-Beuerle and Schuster (n 34), 302–3.

¹⁴¹ For other conflicts with the law applicable to non-contractual obligations see Gerner-Beuerle et al (n 30) (*The Illusion of Motion*), 441–50.

¹⁴² Non-contractual obligations are not defined by the Rome II Regulation, which merely points out that they should be understood as an autonomous concept, see Rome II Regulation, Recital 11.

¹⁴³ It is not clear in all Member States whether the law accords shareholders a dual role depending on the type of loss suffered, although this seems to be the case at least in the Member States where case law on the issue exists, for example in France (Cass. com., 1 April 1997, *Bull. Joly Sociétés* 1997, p. 650, comment by J.F. Barbièri; Cass. crim., 13 December 2000, *Bull. Joly Sociétés* 2001, p. 497). The GEDIP proposal (n 76), also does not distinguish between shareholders that suffered a direct or a reflective loss, but suggests that the claim of either shall be governed by the *lex societatis*.

of harmful act, with an application of the *lex societatis* if the act consists in the exercise of corporate power.¹⁴⁴

In defining the boundary between the *lex societatis* and the *lex loci delicti*, any approach needs to be informed by, and needs to be compatible with, the interpretation of the relevant provisions in the Rome II Regulation and the Recast Brussels Regulation. The former provides that '[n]on-contractual obligations arising out of the law of companies ... regarding matters such as ... the personal liability of officers and members as such for the obligations of the company or body' shall be excluded from Rome II.¹⁴⁵ The latter establishes special jurisdiction of 'the courts for the place where the harmful event occurred or may occur' in matters relating to tort¹⁴⁶ and 'as regards a dispute arising out of the operations of a branch, agency or other establishment, in the courts for the place where the branch, agency or other establishment is situated'.¹⁴⁷

The first approach is in line with some proposals on the harmonisation of private international company law.¹⁴⁸ It is also the approach that seems to correspond most closely to those taken in the Rome I and Rome II Regulations. Insofar as this approach does not classify breaches of company law duties as tort law, it would probably also be in line with the opinion of the Court of Justice, which decided in *Holterman* that liability claims based on a breach of directors' duties does not fall within the special tort jurisdiction of the Brussels Regulation.¹⁴⁹ The Court of Justice held that where 'a company sues its former manager on the basis of allegedly wrongful conduct, Article 5(3) of Regulation No 44/2001 [dealing with jurisdiction for tort claims¹⁵⁰] must be interpreted as meaning that that action is a matter relating to tort or delict where the conduct complained of may *not* be considered to be a breach of the manager's obligations under company law'.¹⁵¹ Instead, claims brought by the company and based on a breach of company law duties are considered by the Court of Justice to fall under what is now Article 7(1) of the Recast Brussels Regulation.

Furthermore, a correspondingly broad interpretation of the *lex societatis* would not impose undue disadvantages on injured parties seeking to enforce a claim. The majority of cases are likely to involve claims based on a breach of director's duties, which are usually owed to the company, rather than to outsiders. In other cases, the special jurisdiction of the court for the

¹⁴⁴ For details of the national laws see Gerner-Beuerle et al (n 29), 121.

¹⁴⁵ Article 1(2)(d) Rome II Regulation.

¹⁴⁶ Art. 7(2) Recast Brussels Regulation.

¹⁴⁷ Art. 7(5) Recast Brussels Regulation.

¹⁴⁸ Art. 3(1), no. 8 of the Sonnenberger proposal (n 77), stipulates that the *lex societatis* shall govern, *inter alia*, 'liability arising from the breach of duties imposed by company law'.

¹⁴⁹ C-47/14 *Holterman Ferho Exploitatie BV v Spies von Büllsheim* ECLI:EU:C:2015:574.

¹⁵⁰ Now Art 7(2) Recast Brussels Regulation.

¹⁵¹ *Holterman* (n 149), para 79 (emphasis by us).

place where the harmful event occurred¹⁵² would not be available (as such claims would not be classified as tort law). However, where the injured party is not located in the home jurisdiction of the company, the behaviour giving rise to the liability action will presumably often be connected with the operations of an establishment of the company in the host state. The injured party would therefore be entitled to sue in the courts of the host state pursuant to Article 7(5) Recast Brussels Regulation.

On the other hand, the first approach has the disadvantage that it may lead to the cumulative application of two liability regimes if the director's conduct constitutes both a breach of company law and of general tort law *and* the place where the damage occurs pursuant to Article 4(1) Rome II Regulation is not in the country where the company is registered or incorporated (provided the *lex societatis* is determined according to a variant of the incorporation theory, as assumed here). In addition, the classification may depend, at least to some extent, on the formulation of the Member States' internal company law and directors' duties. Yet, it is unlikely that this problem will create major inconsistencies in the classification of the relevant social conflicts between Member States. In most cases, it should be possible to arrive at an autonomous understanding of 'company law' for purposes of private international law by defining what belongs to company law independently from the classifications of internal law and in contradistinction to neighbouring areas of private international law, especially insolvency law and securities regulation. In this way, for example, liability for misstatements made in disclosures required under capital markets or takeover law or liability for entering into obligations that the director knows the company will not be able to perform would be excluded from the scope of the *lex societatis*, even if the corresponding obligations were set out in the internal company law. Likewise, where a Member State relies on provisions of general tort law for the regulation of directors' duties, the application of these rules would effectively be restricted to domestic companies.

The second possible solution, a distinction according to the type of injured party (and presumably also according to the type of loss suffered), would have the advantage that it presents at first sight a relatively clear criterion that allows a functional demarcation between the *lex societatis* and the *lex loci delicti* not dependant on the internal delineation of company law and tort law. It also seems to be the preferred solution of the GEDIP proposal, which suggests that 'the liability in tort of the members and directors of a company vis à vis third parties' shall be excluded from the scope of a proposed regulation.¹⁵³ The recitals would clarify that the exclusion applied to liability 'in particular resulting from misrepresentation or undercapitalisation', which would instead be governed by the Rome II Regulation.¹⁵⁴ Thus, a

¹⁵² Art. 7(2) Recast Brussels Regulation.

¹⁵³ GEDIP proposal, Art. 2(a).

¹⁵⁴ GEDIP, 'Vingt-cinquième réunion, Luxembourg, 18-20 septembre 2015, Compte rendu des séances de travail', available at <https://www.gedip-egpil.eu/reunionstravail/gedip-reunions-25.htm>, at I 1.1.

bright line rule is envisaged that includes liability to the company and the shareholders¹⁵⁵ and excludes liability to third parties. Notably, this solution does not distinguish between direct and indirect (reflective) loss but proposes to qualify shareholders always as parties governed by the *lex societatis* and never as third parties.

However, there are good reasons not to choose a bright line rule as in the GEDIP proposal. First of all, it is clear that a consideration of the type of behaviour that gives rise to liability is unavoidable. A director who commits a tortious act in an entirely private capacity, i.e. who neither exercises corporate powers nor acts in any way within the sphere of corporate activity, will evidently not be liable pursuant to company law but pursuant to tort law, even if the injured party happens to be a shareholder of the director's company. More ambiguously, but still relatively well established in the Member States, a director who misrepresents facts in disclosures to investors who purchase or sell the company's shares as a consequence of the misrepresentation is also liable to the investors under tort law.¹⁵⁶ If a certain substantive assessment of the defendant's behaviour is therefore inherent in the test, it is not clear why shareholders who complain of the violation of an individual right and suffer a loss that is not only a reflection of the loss incurred by the company should be treated differently from other parties injured by the tortious acts of directors. Shareholders and third parties are, in the above examples, in the same position, and presumably the policy decisions underlying the provisions of internal law that apply in these cases will take account of the difference in position between such claimants (both shareholders and non-shareholders) on the one hand and shareholders suffering a reflective loss on the other. If this is correct, it is accordingly more convincing (assuming this second solution is adopted) to delineate the *lex societatis* and the *lex loci delicti* not simply pursuant to the type of injured party, but by asking whether the claimant has suffered a loss (1) as a result of the violation of an individual right *and* (2) the loss is not only a reflection of the loss suffered by the company.

Once this substantive assessment is injected into the test, the ostensible advantages in terms of legal certainty compared to the first approach are no longer apparent. In particular, the scope of the *lex societatis* would be defined pursuant to the open-ended terms 'acting within the sphere of corporate activity' (or a comparable formulation) and 'individual right' (and correspondingly, 'third party'). It should be noted that these terms will not depend on their understanding by national courts and policy makers. As part of the conflict rule of a future Rome V Regulation, they would become concepts of EU law and would consequently need to be interpreted autonomously. Thus, there would be no risk of shifting boundaries between the *lex societatis* and the *lex loci delicti*, irrespective of differences in understanding in the

¹⁵⁵ GEDIP proposal, Art. 5(g).

¹⁵⁶ This has been decided in a number of countries, especially in the wake of the dotcom bubble in the early 2000s, see for example in Germany BGHZ 160, 134 (*Infomatec I*); BGHZ 160, 149 (*Infomatec II*); and in France Cass. com., 22 November 2005 (*Sté Eurodirect marketing c/ Pfeiffer*), *RTD com.* 2006, p. 445. The GEDIP proposal (n 154) also seems to have this situation in mind when it argues that liability 'resulting from misrepresentation ... should be governed by Rome II'..

Member States' internal laws, for example, of the definition of an individual right of the shareholders as opposed to a right they hold *qua* shareholder.

Nevertheless, a broad formulation of directors' duties would allow Member States to bring a provision designed to regulate the behaviour of company directors relatively easily within the reach of the host state law (where injured parties are located¹⁵⁷), and the host state could accordingly impose part of its liability regime on the directors of foreign companies operating within its territory. For example, a formulation of directors' duties as in the French Commercial Code, which provides that directors shall be liable 'to the company or third parties either for infringements of the laws or regulations applicable to public limited companies, or for breaches of the memorandum and articles of association, or for management mistakes'¹⁵⁸ would presumably need to be characterised as tort law according to the second approach if the claimant is a third party. In other words, following a functional approach, this provision is then to be characterised as either *lex societatis* or *lex delicti* according to which party suffers the damage.

To what extent this classification would lead to overreaching host state law would depend crucially on the conditions that gave rise to liability under national law. Pursuant to the current situation in France, liability to third parties (understood as not including the shareholders) requires a so-called *faute séparable des fonctions* (a fault separable from the functions of the defendant director). *Faute séparable* was described by the Cour de Cassation as 'an intentional fault of a particular gravity that is incompatible with the normal exercise of the director's corporate functions.'¹⁵⁹ This can arguably be equated with a tortious act and may, therefore, justify the tort-law classification for purposes of private international law. However, it should be noted that the concept is case-law based and its contours are evolving. In more recent case law, the courts seem to be willing to acknowledge that an action may constitute a *faute séparable* even where the directors exercise their corporate powers, for example to approve financial accounts that are materially misleading.¹⁶⁰ Thus, it is clear that this approach to classification leads to a potentially broad scope of application of the host state's law, including in matters that fall within the core area of managerial activity, such as the approval of the company's accounts.¹⁶¹ If a third party sues, this approach would lead to the risk that two or more liability regimes applied cumulatively, namely the incorporation state's company law and the tort laws of all countries where the damage occurred.

¹⁵⁷ Art. 4(1) Rome II Regulation.

¹⁵⁸ French Commercial Code, Art. L225-251 (our emphasis).

¹⁵⁹ Cass. com., 20 May 2003 (*Sté d'application de techniques de l'industrie (SATI)*), Bull. Joly Sociétés 2003, p. 786 (our translation).

¹⁶⁰ Cass. com., 10 February 2009, appeal n° 07-20445 (*Société de gestion Pierre Cardin c/ Société MMS International*).

¹⁶¹ Furthermore, the scope of application of the host state law may be extended relatively easily through targeted amendments of internal company law.

Finally, while the third approach mentioned above will in many cases lead to similar results as the first approach, it has the disadvantage that the exercise of corporate power may depend on the scope of that power as defined in the Member States' internal company laws. The boundaries between the *lex societatis* and the *lex loci delicti* may consequently shift from one Member State to another. In addition, as opposed to the first approach, by referring to the exercise of corporate power, it suffers from an inherently unclear criterion that will be difficult to define at the European level. Notably, if the criterion was interpreted as implying that the directors must have acted within the scope of actual powers conferred on them, it would fall short of capturing all situations relevant for company law, for example a breach of the duty to act within powers. Legal uncertainty could also exist where a Member State attaches liability under tort law to inaction by the director. On the other hand, the term 'exercise of corporate power' is presumably narrower than the criteria that apply pursuant to the first approach (breach of directors' duties, the articles or company law) and would therefore combine an ill-defined connecting factor with the risk of a cumulation of the *lex societatis* and the *lex loci delicti*.

In line with the first approach we therefore propose that a future Rome V Regulation should stipulate that the *lex societatis* shall govern the liability of directors for breaches of the company's constitution (the articles of association), directors' duties and company law. It may also be useful to give examples in the recitals of situations where liability does not fall within the autonomous concept of 'company law' that is used to determine the applicable law in order to guide the development and interpretation of this autonomous term.

(iv) Employee participation in company bodies

The composition of the administrative organs of the company, the board of directors in one-tier board systems and the management board and supervisory board in two-tier systems, is a central aspect of company law and, accordingly, all legal systems qualify it as part of the *lex societatis*.¹⁶² In some Member States, commentators submit that the law should allow for an exception from this clear rule as far as employee participation at board level is concerned, since rules that establish, for example, a system of co-determination pursue specific societal goals linked to the place where the company's operations are located and, consequently, where the employees' interests are affected. The exception is suggested to be implemented either by relying on the real seat instead of the incorporation law for the specific case of employee representation or regarding the employee participation regime as overriding mandatory provisions that apply notwithstanding a foreign *lex societatis*.¹⁶³ Another possible option is to exclude the topic of employee co-determination from the scope of a future Rome V Regulation.

¹⁶² See also (i), above.

¹⁶³ Eg in Germany: Hans-Friedrich Müller, in Gerald Spindler and Eberhard Stilz (eds), *Aktiengesetz* (4th edn, Munich: Beck 2019), section on 'Internationales Gesellschaftsrecht' para 32.

Considering the actual legal situation in the Member States, all aspects of board composition, including the involvement of employees, are governed by the *lex societatis*.¹⁶⁴ Furthermore, no court in the Member States has so far been prepared to impose the host state's employee participation requirements on foreign, EU-incorporated companies. It would also be impracticable to incorporate the host state's rules on co-determination into a foreign corporate governance regime, since a wide array of rules ranging from board structure to appointment and removal rights would need to be adjusted. This would inevitably lead to friction between the home and host state corporate governance regimes and, hence, to legal uncertainty. Moreover, the EU rules on cross-border mergers and the European Company (SE) operate under the implicit assumption that employee participation forms part of the *lex societatis*, while also setting up an elaborate negotiation system as a compromise solution.¹⁶⁵ These rules may, of course, effectively result in foreign employee participation rules affecting the board composition of 'domestic' companies, but this may be addressed by harmonising the relevant rules of the *lex societatis*, rather than by excluding the question from its scope.

Nevertheless, it is also worth pointing out that employee participation rules not only address the internal affairs of the company, but reflect wider policy goals as these rules seek to balance the interests of different social actors within the society where a company operates.¹⁶⁶ Therefore, the question arises as to whether the legitimate interests of the host state can justify the imposition of a domestic employee participation system on foreign-incorporated companies. Within the confines of the Treaty, Member States are entitled to protect such social policy goals also in relation to companies governed by a foreign *lex societatis*, for example by relying on overriding mandatory provisions. In this regard, all additional requirements imposed on companies incorporated in another EU Member State are subject to *Gebhard*¹⁶⁷ justification. Given the strict conditions for a justification under *Gebhard*, however, it seems unlikely that the Court of Justice would find an application of the host state's board-level employee participation regime to foreign companies to be compatible with the freedom of establishment.¹⁶⁸

¹⁶⁴ For details see Gerner-Beuerle et al (n 29), 79–99.

¹⁶⁵ Art 133 of Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law (formerly, Art 16 of Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies), which in effect assigns this question to the *lex societatis*. For the negotiation system see Council Directive 2001/86/EC of 8 October 2001 supplementing the Statute for a European company with regard to the involvement of employees.

¹⁶⁶ See, eg, Harry W Arthurs and Claire Mummé, 'From Governance to Political Economy: Insights from a Study of Relations between Corporations and Workers', in Cynthia A Williams and Peer Zumbansen (eds.), *The Embedded Firm* (Cambridge: Cambridge University Press 2011).

¹⁶⁷ C-55/94 *Reinhard Gebhard v. Consiglio dell'Ordine degli Avvocati e Procuratori di Milano* [1995] ECR I-04165.

¹⁶⁸ See, eg, Georg Eckert, *Internationales Gesellschaftsrecht* 346 (Vienna: Manz 2010); Manfred Weiss and Achim Seifert, 'Der europarechtliche Rahmen für ein „Mitbestimmungserstreckungsgesetz“' (2009) *Zeitschrift für Unternehmens- und Gesellschaftsrecht* 542.

Considering the current state of the Court of Justice's case law and in order to attain a reasonable level of legal certainty, a future Rome V Regulation should preferably clarify that all internal governance matters, including board structure, the composition of corporate boards, and the involvement of employees at board level, shall fall within the scope of the *lex societatis*, unless specific social policy reasons justify, according to the *Gebhard* test, the classification of national rules on board composition as overriding mandatory provisions. However, we also recognise that this question may be of a highly political nature and that an exclusion from the scope of the future instrument might offer an alternative solution, as suggested by the European Commission.¹⁶⁹

C. Should harmonisation also extend to companies from third countries?

A future Rome V Regulation would apply to all Member States but, in principle, not to Ireland and Denmark. According to Protocols No 21 and No 22 to the TFEU, Denmark and Ireland do not participate in measures adopted pursuant to Title V of Part Three of the TFEU.¹⁷⁰ The protocol for Ireland provides that it could in principle opt in, while Denmark does not currently¹⁷¹ participate in Union legislation covered by Title V of Part Three of the TFEU.¹⁷² The Danish situation would therefore be virtually the same as the situation of the EEA countries Iceland, Liechtenstein and Norway. The EEA Agreement includes provisions on the freedom of establishment (arts 31 to 35) which mirror those of the TFEU. Thus, as far as the harmonisation of conflict of laws rules considers these provisions and the corresponding case law of the Court of Justice, the situation of these four countries would in practice be similar to the one in the (other) EU countries. In addition, it is possible that future bilateral agreements could provide similar rules.

A different question from the one discussed in the previous paragraph is whether a future Rome V Regulation would, according to its own provisions, cover companies from third countries. Since the Lisbon Treaty, such an extraterritorial approach would indeed be possible for conflict of laws rules. As summarised by Xandra Kramer:

‘It is noteworthy that the proper functioning of the internal market is still mentioned in Article 81(2) TFEU, but no longer seems to be a strict requirement for the purpose of private international law measures, as is evidenced by the addition of the word “particularly”. Within the context of

¹⁶⁹ See Section II.B., above.

¹⁷⁰ See Protocol (No 21) to the Treaty on the Functioning of the European Union, Art. 1 (Ireland); Protocol (No 22) to the Treaty on the Functioning of the European Union, Art. 1 (Denmark). Initially the Protocol (No 21) also applied to the UK which has become obsolete since the UK’s departure from the EU.

¹⁷¹ Denmark has the right to adopt an ‘opt-in system’ substantially similar to Protocol No 21; see Art. 8 of Protocol No 22 and Annex to Protocol No 22. However, given the negative results of the 2015 referendum on this matter, it seems unlikely that Denmark will make use of this right in the near future.

¹⁷² See Arts. 1 and 2 of Protocol No 22.

negotiations on specific existing instruments, in particular the Rome II Regulation, the international market requirement under Article 65 EC was debated in view of the “universal” territorial scope of this instrument (expanding to non-EU torts, parties, and laws). However, eventually it was not regarded an obstacle’.¹⁷³

It can also be noted that both the Rome I and II Regulations state that ‘any law specified by this Regulation shall be applied whether or not it is the law of a Member State’.¹⁷⁴ For the matters discussed in this paper, GEDIP suggests a corresponding universal rule, namely that ‘unless provided otherwise, any law specified by this Regulation shall be applied whether or not it is the law of a Member State’.¹⁷⁵ By contrast, the 1968 EC convention only included companies ‘established in accordance with the law of a Contracting State’ – and, in addition, gave contracting states the option not to apply the convention to companies that had ‘no genuine link with the economy’ of the territories of one of the contracting states.¹⁷⁶

The universalist position by GEDIP can be related to a ‘Savignian’ position of private international law according to which it is possible to establish the applicable law in a neutral way.¹⁷⁷ In the literature, Eva-Maria Kieninger even considers the extension to third countries as one of the main reasons for an EU codification of conflict of laws rules applicable to companies, arguing that the case law of the Court of Justice – interpreting the freedom of establishment of the Treaty – can ‘only’ address intra-EU cases.¹⁷⁸ In addition, Kieninger argues that a lack of such international uniformity would also extend to the European level, since a company incorporated in a third country that has its principal place of business in the EU might be categorised differently in different Member States.¹⁷⁹

However, the general neutrality assumption of private international law may not be fully justified in the present case since accepting a company as established under the law of a non-EU country¹⁸⁰ can have wide-reaching implications for the protection of shareholders, other stakeholders and society at large. In particular, complete universality may be worrying in so far as it would also cover mere letterbox companies established anywhere in the world.¹⁸¹ A radical solution would therefore be to completely exclude third countries from the scope of

¹⁷³ Kramer (n 71), 7 (footnotes omitted).

¹⁷⁴ Art. 2 Rome I Regulation; Art. 3 Rome II Regulation,

¹⁷⁵ Art. 2 GEDIP proposal.

¹⁷⁶ Arts. 1 and 3 EC Convention 1968 (n 79).

¹⁷⁷ See references in note 39, above.

¹⁷⁸ Eva-Maria Kieninger, ‘The Law Applicable to Corporations in the EC’ (2009) 73 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 607 at 618-9.

¹⁷⁹ Ibid at 624.

¹⁸⁰ The same would apply to the choice of a non-state law such as the EMCA (see note 65 above). Note that the choice of non-state laws is even excluded in Art. 3 of the Rome I Regulation as the applicable contract law.

¹⁸¹ For letterbox companies see references in note 26 above.

a future Rome V Regulation. This seems to be the Commission's preferred option.¹⁸² Indeed, it may be politically opportune as Member States may be unwilling to include companies from third countries in the regulation. Conceptually, it could at least draw on the precedent of the Insolvency Regulation Recast, which states that the centre of the debtor's main interest needs to be located in the EU.¹⁸³

It is, however, also possible to develop intermediate solutions. Three options may be available: first, a future Rome V Regulation could enable Member States to *opt into* a wide scope of application that includes the relationship to all third countries (which, in practice, may in the first instance be used by the traditional incorporation theory countries) or at their own choice just to certain third countries. This would have the advantage that, as far as Member States do opt in, it would provide the legal certainty that a common set of conflict of laws rules applicable to all companies typically envisages.¹⁸⁴

In the second option, the starting point would be reversed: the Rome V Regulation would apply to companies from third countries, which were to be recognised as such by any Member State. However, Member States could be allowed to *opt out* of the Regulation for companies incorporated in all or specific third countries.¹⁸⁵ At a later review of the Regulation, it could then be determined to what extent Member States have made use of the opt-out and whether there was any need for change or adjustment. Alternatively, it could be provided that Member States can make use of overriding mandatory rules and other mechanisms to protect public interests in a wider set of scenarios than in relation to EU/EEA-incorporated companies.

A third suggestion is to introduce an explicit process for accepting companies from third countries for purposes of conflict of company laws, similar to the equivalence decisions in other areas of EU harmonisation such as accounting law.¹⁸⁶ In particular, this may be a feasible solution as far as the company laws of other OECD countries are concerned, as well as countries with whom the EU has agreed on free trade agreements.¹⁸⁷

These three intermediate options would make it possible to extend EU-mandated choice of law to third countries, subject to the necessary safeguards. If the EU follows this approach, it

¹⁸² See Section II.B, above.

¹⁸³ Insolvency Regulation Recast, recital 25.

¹⁸⁴ These rules could then also be interpreted by the Court of Justice which, if appropriate, may well differentiate between the relationship to other Member State and third countries (as may also happen for the Rome I and II Regulations, e.g., for the application of the concept of *ordre public*).

¹⁸⁵ Opt-outs are also used elsewhere in EU law, see eg Art. 12 of the Directive 2004/25/EC of the European Parliament and the Council of 21 April 2004 on takeover bids.

¹⁸⁶ See Commission Regulation (EC) No 1569/2007 of 21 December 2007 establishing a mechanism for the determination of equivalence of accounting standards applied by third country issuers of securities pursuant to Directives 2003/71/EC and 2004/109/EC of the European Parliament and of the Council.

¹⁸⁷ For the impact of free trade agreements on corporate mobility see Karsten E Sørensen, 'Free Movement of Companies under the New EU Free Trade Agreements' (2016) *European Company Law* 46.

would then also make sense to engage with third countries through the Hague process.¹⁸⁸ Thus, in the medium/long term the aim may be to develop a new convention that provides for internationally uniform conflict of laws rules applicable to companies. However, this long-term prospect should not speak against a Rome V Regulation, which may well be a ‘stepping stone’,¹⁸⁹ towards such international rules.

V. Conclusion

This paper has shown significant legal variation and uncertainty in the conflict of laws rules of the Member States applicable to companies. This variation constitutes an obstacle in the creation of a single market. Therefore, the main recommendation of this paper is that the EU should harmonise private international company law in the EU. While the case law of the Court of Justice on the freedom of establishment has clarified some questions, it is also evident that case law cannot provide for the same level of legal certainty as codified conflict rules.

In substance, we suggest that the main connecting factor of a future ‘Rome V Regulation on the Law Applicable to Companies’ should be based on the ‘incorporation theory’. Thus, a company should be governed by the law according to which it has been incorporated, and an unincorporated entity by the law according to which it has been formed.

Risks of positive and negative conflicts of the applicable rules arise from differences across the Member States as to the scope of the *lex societatis* and other areas of law with distinct connecting factors. Such differences are likely to be unavoidable to some extent. A duty to recognise foreign entities according to their own company law generates the risk that domestic norms of the host state that have the aim of protecting local interests may be disapplied. Host states can, therefore, have a legitimate interest to address those local interests through rules and principles not classified as ‘company law’ and not falling within the *lex societatis* for purposes of conflict of laws. In order to ensure that a future Rome V Regulation has a uniform scope of application and guide an autonomous interpretation of the regulation, we argue that the regulation should provide for a non-exhaustive enumeration of the matters governed by the applicable law.

A challenging question is how a future regulation would relate to existing EU conflict of laws rules. This paper suggests that legal mechanisms designed to address problems arising specifically in insolvency or in the vicinity of insolvency should not be included in the scope of the *lex societatis*, irrespective of the internal classification of the provision in the Member

¹⁸⁸ For the engagement of the EU in the Hague process see also Jan-Jaap Kuipers, *EU Law and Private International Law* (Leiden: Martinus Nijhoff 2012), 16–8.

¹⁸⁹ Cf John Ravenhill, ‘Regional Trade Agreements’ in John Ravenhill (ed), *Global Political Economy* (3rd edn, Oxford: Oxford University Press 2011), 202–6 (for question whether growing regionalisation is a ‘stepping stone’ or a ‘stumbling block’ for international integration).

State's company or insolvency law. Such mechanisms are in particular legal provisions that derogate from common rules of civil and commercial law to protect the interests of the general body of creditors and mitigate risk-shifting in the vicinity of insolvency. However, in contrast to the case law of the Court of Justice interpreting the scope of the Insolvency Regulation, it would be irrelevant for the functional determination of the boundary region between company law and insolvency law suggested here whether the action in question was in fact brought by the liquidator in the context of insolvency proceedings.

With respect to companies from third countries, the Commission seems to favour a solution that would exclude all such companies from a future regulation on the law applicable to companies. Yet, this would create tension between this new regulation and the existing Rome regulations that follow the conventional approach of private international law in providing for universal rules. This paper has suggested some intermediate solutions that would accommodate these tensions. It has also pointed out that this issue should be a matter of international cooperation or even international harmonisation. Indeed, given the global reach and mobility of large companies, the topic of this paper is bound to remain significant and topical in the foreseeable future.

European Corporate Governance Institute

about ECGI

The European Corporate Governance Institute has been established to improve *corporate governance through fostering independent scientific research and related activities.*

The ECGI will produce and disseminate high quality research while remaining close to the concerns and interests of corporate, financial and public policy makers. It will draw on the expertise of scholars from numerous countries and bring together a critical mass of expertise and interest to bear on this important subject.

The views expressed in this working paper are those of the authors, not those of the ECGI or its members.

European Corporate Governance Institute

ECGI Working Paper Series in Law

Editorial Board

Editor	Amir Licht, Professor of Law, Radzyner Law School, Interdisciplinary Center Herzliya
Consulting Editors	Horst Eidenmüller, Freshfields Professor of Commercial Law, University of Oxford
	Martin Gelter, Professor of Law, Fordham University School of Law
	Geneviève Helleringer, Professor of Law, ESSEC Business School and Oxford Law Faculty
	Curtis Milhaupt, Professor of Law, Stanford Law School
	Niamh Moloney, Professor of Law, Department of Law, London School of Economics and Political Science
Editorial Assistant	Úna Daly, ECGI Working Paper Series Manager

<https://ecgi.global/content/working-papers>

European Corporate Governance Institute

Electronic Access to the Working Paper Series

The full set of ECGI working papers can be accessed through the Institute's Web-site (<https://ecgi.global/content/working-papers>) or SSRN:

Finance Paper Series <http://www.ssrn.com/link/ECGI-Fin.html>

Law Paper Series <http://www.ssrn.com/link/ECGI-Law.html>

<https://ecgi.global/content/working-papers>