ACKNOWLEDGMENTS

This chapter is based partly on the author's own observation and research, and partly on information and opinions received from a number of collaborators, whose authority he has in many instances accepted without forming an independent opinion on the question. Questionnaires on the principal points were submitted to collaborators in the various countries of the Common Market; the answers, along with information from other sources, were compiled in a draft which was submitted to the same or other collaborators, and revised in response to their comments. It was impossible to have the manuscript read in its final form by the collaborators, who therefore have no responsibility for errors of fact or of judgment which may appear in it.

The principal European collaborators are the following: (in alphabetical order)

Mr. Ernest Arendt, Advocate, of Luxembourg, Lecturer at the University of Nancy, who read and criticized the entire manuscript.

The late Professor Tullio Ascarelli, of the University of Rome, who assisted greatly in the preliminary planning of the study, answered a large number of questions regarding Italian law, and read and criticized a part of the manuscript before his untimely death in November, 1959.

Professor Giorgio Bernini, of the University of Ferrara, who answered a part of the questionnaire covering Italian law.

Mr. P. Bruna, Advocate, of Rome, who read and criticized the entire manuscript.

Mr. J. E. J. Deelen and Mrs. A. C. van der Vlis, of Amsterdam, who answered the questionnaire covering Netherlands law, and who read and criticized a part of the manuscript.

Professor Jacques Heenen, of the University of Brussels, who answered the questionnaire covering Belgian law, and who read and criticized the entire manuscript.

Professor Roger Houin, of the University of Paris, who answered the questionnaire covering French law, and read and criticized the entire manuscript.

Professor Rolf Serick, of the University of Heidelberg, who answered the questionnaire on German law, and who read and criticized a part of the manuscript.

In addition, the author wishes to mention with appreciation Mr. Chiomenta, Advocate, of Rome, who arranged for the work of Mr. Bruna, Mr. Bernard Delvaux, Advocate, of Luxembourg, who supplied documentary information, and Professor Isaac Kisch, of Amsterdam, who arranged for and reviewed the work of Mr. Deelen and Mrs. van der Vlis. Other persons, too numerous to be mentioned here, gave the author invaluable information on the operations of their own business enterprises, and on their own professional experiences.

INTRODUCTION

The emerging Common Market of Western Europe calls for new organization planning by many American enterprises. Many who have never before maintained a European organization will now develop one; and those who have long had European organizations will have to re-examine and revise them.

The subjects of planning—licenses to do business, liabilities of owners, taxation, management, finance—are the same in the Common Market as anywhere else. But there are many ways in which the European variables differ radically from those in the United States; there are others in which the variables in the Common Market will be found to differ significantly from those which prevailed in compartmented Europe.

In the following pages we will review some of the considerations which affect business organization in the European Economic Community, emphasizing the considerations which, on this new business frontier, are most different from corresponding considerations in the United States.
I. DOING BUSINESS FROM THE OUTSIDE (WITHOUT "ESTABLISHMENT")

Most of the present essay will be concerned with the organization of branches and subsidiaries in Europe. But branches and subsidiaries are not the only means of doing business in Europe; some of the largest exporters and importers may get along without them. These traders may do business with no one at all representing them in Europe; or with agents of various kinds who fall short of the "branch" category—who do not create, in the European term, an "establishment" of the American company. In the next few pages we will indicate the principal considerations which might lead an enterprise to avoid creating a European "establishment," although doing business with Europe; we will also indicate by what means the enterprise could do business without "establishment."

A. FREEDOM OF ENTRY

I. PROVISIONS DIRECTED ESPECIALLY AGAINST FOREIGNERS

A good deal of attention is devoted in the Treaty of Rome and in current European discussion of it to the right of a national of one country to open a business establishment in another country on a plane of equality with the latter's own nationals. A good deal of this discussion is of very minor importance to Americans, because it concerns the right of individuals to live and work in the second country—a matter which Americans associate with the word "immigration." Among the European countries, the right of an individual Dutchman to operate a machine shop in Antwerp, or of an individual Italian to operate a tailor shop in Paris presents very important questions of economic and political policy.

The interest of American enterprises in the Common Market is generally of a different kind. They do not seek primarily to employ American citizens in Europe, but to employ American processes, products, trade names, and money. Although they would often like

---

1 Although this word is not common as a legal term in American domestic law, it has long been used in the English language version of treaties of "Friendship, Commerce, and Navigation." See Walker, Modern Treaties of Friendship, Commerce, and Navigation, 42 MINN. L. REV. 805 (1958). It appears in the title of the recently concluded "Convention on Establishment" with France, November 25, 1959, 41 DEPT STATE BULL. 829. The corresponding European terms are établissement, Niederlassung, stabilimento, and vestiging.
to use a few Americans as resident executives or technicians in their foreign subsidiaries, they can usually manage without.

We will notice briefly the rights of individual foreigners to conduct or work in a business in European countries, even though this is not a matter of primary concern. In France and Belgium foreign individuals must obtain a license to do business as permanent residents, called a *carte de commerçants étranger.* These are said to be fairly easily obtained in France (although one must wait a few months and wheedle a few officials), but traditionally difficult to obtain in Belgium. In France, Americans can probably demand the eventual issue of the *carte* under the terms of the newly signed Convention of Establishment between the two countries, but the right which this treaty creates will probably not cause the *carte* to pass through official channels any faster than it did before.

The Convention of Establishment lists only the following lines of business, in which Americans shall not have the same rights as Frenchmen to do business in France:

- Communications
- Air or water transport
- Banking involving depository or fiduciary functions
- Exploitation of the soil or other natural resources
- Production of electricity

The Convention presumably supersedes the earlier French law which purported to admit Americans to exercise private rights to the same extent as the United States offers similar right to Frenchmen, with a limited number of exceptions.

Three other countries of the Market—Germany, Italy, and the Netherlands, apparently have no rules affecting foreign individuals differently from nationals in the matter of access to commerce,
except that Italy has a reciprocity provision. 6 If these countries should adopt discriminatory provisions, they would be inapplicable to Americans because of the treaties of Commerce, Friendship and Navigation ("C.F.N. treaties") subsisting between them and the United States. 7 All three treaties, like the U.S.-French Convention of Establishment, guarantee American individuals the same rights as nationals to carry on businesses in the respective countries. The German and Netherlands treaties contain exceptions similar to those in France, 8 but the Italian treaty makes no such exceptions.

When we turn from the rights of individual Americans to live and work in European countries, and look at the rights of American corporations, we find that they have no less rights than individuals. The C.F.N. treaties give American companies as well as American individuals rights to establish branches and carry on commerce, with the same exceptions for key industries. With Belgium and Luxembourg, the United States has no C.F.N. treaties, but these countries do not attempt to discriminate against foreign enterprise.

If the problem of a license to do business proves troublesome in spite of the rights conferred by treaties between the European Country involved and the United States, there are other treaties affecting the right of establishment which may prove helpful. The three countries of the Benelux union are bound by treaty to admit the enterprises of each other. Therefore, if an American enterprise succeeds in establishing a bona fide subsidiary in one of those three countries, it is entitled to do business in the others. Further, Belgium and Luxembourg have made treaties of Friendship, Commerce, and Navigation with France, so that an entry into France may serve as a means of entry to Belgium or Luxembourg, and vice versa, subject to enumerated exceptions of a few particular lines of business. 9

Further possibilities of entering one country through another

9 The press has reported that a treaty on the same subject is under negotiation with Belgium.
10 One exception in the French treaty—production of electric energy—does not appear in the German and Netherlands treaties, but the others appear in Article VII of both treaties.
arise from the terms of the Treaty of Rome, which created the Common Market. The Council of the Economic Community is enjoined by the Treaty of Rome to "lay down a general program for the abolition of restrictions existing within the Community on freedom of establishment" before the end of the first transitory stage—that is, before 1962.\(^\text{10}\) At the beginning of the second stage (supposedly 1962) the Council will have power to order abolition by majority vote.

The rights which the Council may grant, under the Rome Treaty, to companies of other Community countries cannot be denied merely because the companies are owned by Americans (or other outsiders). A company which is organized under Belgian law, managed in Belgium, and has its biggest plant there, must be treated by France as a Belgian national, for purposes of "establishment."\(^\text{11}\) A literal reading of the Treaty suggests that any one of these three features would give the company Belgian rights, but a leading French commentator has challenged this interpretation.\(^\text{12}\) Hence we do not think it is safe to assume that one can gain any formal advantage out of merely filing corporation papers in Luxembourg, as Americans do in Delaware.\(^\text{13}\) But a company with its true principal office and operational base in one country is sure of the right to set up an establishment in the others under the terms of the directives on establishment which the Community Council may issue.

We conclude that laws which discriminate against Americans in the matter of business licensing present a surmountable problem, or none at all, outside of a limited group of businesses in most of which American corporations are unlikely to be interested. This is not to say that Americans will not encounter discrimination, but merely that the important discrimination will not be in the form of a law requiring special permission for foreign business enterprises. One of the other obstacles may be, in France and Belgium, a law on the licensing of American individuals to be company executives.\(^\text{14}\) More serious obstacles will be presented by the laws on exchange of cur-

---

\(^{10}\) Treaty Establishing the European Economic Community [hereinafter cited as the Treaty] art. 54(1).

\(^{11}\) The Treaty art. 58.


\(^{13}\) Article 58 of the Treaty invites some speculation as to whether national rights can be obtained by maintaining a mere "registered office"; this question is examined by Mr. Thomas L. Nicholson in another chapter of this book.

\(^{14}\) Discussed later, in the sub-chapter on "Management."
rency; they do not discriminate against American companies, but only against American dollars. Although the victim of the discrimination may be the same, the means of dealing with the discrimination may be quite different. Finally, there is the obstacle of laws on business licensing which in terms apply equally to citizens and to foreigners, but which may be administered to discriminate in fact against foreigners. These non-discriminatory licensing laws will be next discussed.

2. DOMESTIC LICENSING PROVISIONS

When an American enterprise surmounts the hurdle of foreign nationality, it has only scratched the surface of the problem of establishing itself in Europe. It must still cut through the mass of licensing requirements which apply equally to locally owned enterprises. In Luxembourg and the Netherlands every business establishment must be licensed, whether foreign or domestic. In Italy, a permit is required for every retail trade, but not for manufacturing or (apparently) wholesale commerce. In Germany, access to manufacturing and wholesale trades is free, but every retail establishment requires a license. In France, entry into commerce is theoretically free, but there are a host of kinds of business for which licenses are required; a recent study reported the following list, which was not claimed to be complete, of products in which dealers must be licensed by one authority or another:

Matches, arms, and explosives
Drugs
Gas generating equipment
Transportation
Amusements and spectacles
Meat, milk, livestock, fish
Bakery goods
Wines

In addition, the following enterprises must be licensed, regardless of products:

General stores
Single-price stores (comparable to "5 and 10 cent stores")
Stores specializing in close-outs
Brokerage of several kinds—e.g., stock, foreign exchange, and ships

15 Discussed later, in the sub-chapter on "Financing," and also in the separate chapter by M. Fernand Jeantet, under the title "Exchange Control Regulations in France."
Belgium is apparently the country with the greatest freedom of commerce; but licenses are required for dealing in transportation and in certain agricultural products, and a recent law requires proof of professional qualifications in all forms of "small business." Our information on how and why licenses are granted and refused in European countries is very indefinite—as it would be with respect to the United States, and for the same reasons. Lack of technical and financial qualifications will doubtless impede licensing, but they will rarely be the only impediments. Many of the French laws, at least, have added to technical requirements a condition that the proposed establishment should be in "the interest of the national or regional economy." Probably this question would be answered chiefly by reference to national and regional economic plans, either published or nascent. Our French collaborator, Professor Houin, warns that there is no effective judicial remedy against administrative discretion in denying the license for a foreign "merchant" which an American or other foreigner needs to serve as executive of a company or branch in France.

In Italy, the existence of factors other than technical ones is suggested by the membership of the committees which pass on retail licenses; they consist of the mayor, two local merchants, and two local laborers. Although an appeal from the committee's denial lies to an administrative court, the views of competing local interests are likely to color the final decisions.

In the Netherlands, the licensing process involves the advice of nation-wide trade associations which might be expected to view dimly any competition with their own products. There are also reported to be in the Netherlands very widespread "tying agreements," whereby all kinds of concerns engage to buy from only certain sources, which in turn agree to sell only to certain outlets. Thus there is a closed merchandising circuit, in which a newcomer can penetrate only with the consent of the trade associations.

From these fragmentary observations, it is evident that entry into the European market raises very complex problems. Entry is likely to prove extremely difficult in businesses, like the retail trade, in which a large number of local merchants fear new and powerful competition, but quite easy in certain manufacturing industries.

16 This and most of the preceding statements on "domestic licensing provisions" are based on Le Droit d'Établissement, op. cit. supra note 2, at 999, 1004.
where the new products may be exported to compete elsewhere, or where they replace products which were primarily imported before.

None of these impediments to market entry—which apply in theory to local enterprise as well as to American—will be automatically eliminated by the Treaty of Rome, or by treaties of friendship, commerce, and navigation with the United States. These treaties exclude only discrimination against foreigners.

The exclusive agreements between manufacturers and distributors which obstruct entry of newcomers into the market may be contrary to the general principles enunciated in Article 85 of the Treaty. But these principles, like those of American antitrust law, are subject to widely varying interpretations. For the time being, their enforcement depends on the initiative of the Member States, none of which have much prior experience with "antitrust" law. In view of the persistence of trade restraints in the United States 70 years after the Sherman Act, and the traditional stability of distribution patterns in Europe, we would guess that many years will pass before actual penetration of European distribution systems becomes easy.

B. STAGES OF ENTRY

To speak of doing business with Europe from the outside is, of course, a mere metaphor. An enterprise which does any business at all with Europe becomes in some degree involved in European legal problems. To examine our problem more closely we will look at the problem of entering Europe as a problem of a timid bather getting into the swim—he may stand on the shore throwing pebbles, he may dip in his toes, he may wade, he may swim with his head out, or he may take a deep dive. Each stage of immersion involves exposure to added risks, and so does each stage of entry in the European market. We will therefore look at the various degrees to which an

18 The Treaty Article 85 condemns agreements and practices which consist in—(a) the direct or indirect fixing of purchase or selling prices or of any other trading conditions; (b) the limitation or control of production, markets, technical development or investment; (c) market-sharing or the sharing of sources of supply; (d) the application to parties to transactions of unequal terms in respect of equivalent supplies, thereby placing them at a competitive disadvantage; or (e) the subjecting of the conclusion of a contract to the acceptance by a party of additional supplies which, either by their nature or according to commercial usage, have no connection with the subject of such contract.

But the general condemnation is subject to an exception for agreement and practices which do not "eliminate competition in respect of a substantial proportion of the goods concerned," and which "contribute to the improvement of the production or distribution of goods or to the promotion of technical or economic progress while reserving to users an equitable share of the profits resulting therefrom."
American enterprise may enter the European Economic Com­munity, and note some of the legal involvements which attach to each stage of entry.

The stages of entry must be carefully distinguished, because entry for one purpose may not be entry for another. "Establishment" is primarily a conception of commercial law; when an enterprise is "established" by commercial law standards, it is required to file and publish documents regarding its legal structure and its officers, and to enter its name in the commercial register.

However, an enterprise which is "established" for purposes of commercial law is not necessarily established for purposes of tax law. The double-taxation treaties which bind most of the Common Market countries to the United States have greatly restricted the tax concept of establishment; it is now distinctly different from the commercial law concept.

Because of these differences, we will consider the stages of entry into the European market from three different points of view—commercial licensing and registration, tax liability, and liability to suits in European courts. These three incidents may serve to illustrate the host of others which time and space forbid us to examine. Some of the other incidents—involving labor relations, restraints of competition and exchange control—are examined by the authors of other chapters of this book.

I. NO FOREIGN ASSETS

To separate itself as completely as possible from European entanglements an American enterprise may assure itself that it has no assets, tangible or intangible, in Europe. It may, that is, sell only by delivery at U.S. ports, and for payment in U.S. dollars on delivery. Clearly such a company need give no thought to European tax laws or European commercial status. European duties and exchange restrictions may worry the company's European customers, but not the company itself.

Oddly enough, the company might even then be sued in some European courts. European courts do not generally condition jurisdiction on the "presence" of the defendant, as common law courts do. In France and Luxembourg, the codes expressly provide that suit may be brought against a non-resident defendant for contracts undertaken outside the country; all that is needed is that the plaintiff should be a local resident. Italy is only a little stricter, requiring

that the obligation sued on should have been made, or should be due to be performed, in the country.\textsuperscript{20}

Fortunately for American enterprises, suits maintained against a company under such circumstances may do it little harm. If there are no assets in the country where the judgment is rendered, the judgment cannot be executed there. If the plaintiff tries to sue on his judgment in America, he will find that American courts consider it unenforceable for lack of jurisdiction.\textsuperscript{21} Even in Europe, the very countries which grant such judgments refuse to give effect to similar judgments rendered in other countries with similar laws; such judgments are said to be nationally valid, but internationally invalid.\textsuperscript{22}

2. EFFECTS OF FOREIGN ASSETS

The no-asset system may have merit for avoiding European entanglements, but it is not the best way to build up foreign business. Most enterprises will find that, if they want to make money, they cannot help acquiring foreign assets such as accounts receivable and balances in the hands of agents.

Assets abroad, whether tangible or intangible, large or small, will not subject the American owner to European income taxes. Neither do they involve commercial licensing and registration. But they expose the owner to effective suits in European courts. If the defendant has assets in the jurisdiction, he may be sued whether present or not, and the judgment may be executed on the assets that are present. This means that when a company acquires foreign assets, it may be compelled to defend abroad suits arising out of its business, or else abandon the assets.

This liability can be considerably reduced, if the company desires, by employing contract clauses providing for litigation at some other reasonable point, such as the state of the American company's home office. Such clauses are honored generally in Belgium, France, Germany, Luxembourg, and the Netherlands, but not in Italy.\textsuperscript{23} Whether

\textsuperscript{20} Codice di Procedura Civile art. 4(2).
\textsuperscript{21} Restatement, Conflict of Laws, §§ 77, 429-430 (1934).
\textsuperscript{22} As to France, see Batifol, Traité Élémentaire de Droit International Privé 836 (1955).
\textsuperscript{23} Id. at 763-64.

Luxembourg: Our Luxembourg collaborator, Mr. Arendt, calls attention to an exception affecting patents and trademarks. The filing of a patent or trademark in Luxembourg constitutes a consent to litigation affecting the patent or copyright. This consent will prevail over a contract providing for exclusive jurisdiction somewhere else.
they will scare away more business than they are worth we cannot say.

In addition to the possibility of being sued in Europe, a company which has assets there must consider the possibility of having to bring suit there. If it has assets, it may have to protect them. Receivables in particular must sometimes be collected by suit; patents, processes, and trademarks require constant legal protection. Since European laws and procedures are quite different from American, American enterprise will have to rely on European legal counsel. The possibility of having to find and retain such counsel, if the assets are not to be lost, must be reckoned among the costs of owning them.

3. EMPLOYEES IN EUROPE

In the six countries of the European Community a distinction is drawn, much more sharply than in American law, between “salaried personnel” and “commission agents.” As their names suggest, they are commonly differentiated by receiving (on the one hand) a regular weekly or monthly wage, or (on the other hand) a commission based purely on the amount of business transacted. But there are usually more fundamental differences. The salaried personnel are normally full-time employees of the enterprise, owing an undivided loyalty to it alone, and receiving instructions from its management; the “commission agent” is normally free to represent various clients, and chooses his own hours and his own ways of soliciting customers. We will not speculate on the legal status of representatives who fall between the stools; to employ such persons would be to invite juridical uncertainty. We will explore the results of employing persons who fall clearly in one category or the other; and we will start with salaried personnel.

a. Liability to Suit

The mere presence of employees will make no difference in the suability of the employing company unless they hold general powers of attorney to make contracts in the company’s name. This conclusion, perhaps surprising to Americans, follows from the fact that European courts do not base their conceptions of jurisdiction on “presence” of the defendant. However, the presence of employees will probably result in increasing the probabilities of suit. Employees in Europe will probably make more contracts with Europeans, and commit more torts against Europeans, than employees in the United States; and so the probabilities of European litigation will increase.
b. Liability to Commercial Regulation

The presence of employees will affect the incidence of commercial regulations in varying ways, depending on the permanence of the employees' stay, and the extent of their powers. We can say broadly that the temporary presence of employees, even though they come exclusively on business, will not in itself subject the company to European commercial licensing or registration. What is "temporary" is not easily defined, but the periods for which an American may reside as a tourist without visa—usually about three months—offer a general guide.

The consequence of employees' residing more permanently in Europe are viewed differently by our different informants. Professor Houin, speaking for France, observes, "It is hard to see how a company could have salaried personnel permanently in France and in charge of the company's affairs without having a French establishment; a physical place of business is not the test of establishment." His conclusion is that a company with employees in France—beyond the duration of tourist visas—is obliged to register itself as "established" in France. Our Belgian and German informants, on the other hand, do not see any commercial problem in the employees' presence if they do not have powers of contracting for the company. It would appear that in the latter countries permanent representatives could furnish information on products, especially technical information, and could supply maintenance service (without remuneration from customers) without commercially registering the company. Probably they could do so even in France if the evidence were sufficiently clear that that was all they were doing.

Commercial regulation becomes important when contractual negotiation—buying, selling, or licensing—is carried on by employees on a continuing basis. Our collaborators indicate that commercial qualification is definitely not required for casual and occasional representation; but it may be when a continuous practice of dealing develops.

What is "dealing," for this purpose? Professor Heenen advises that it does not include (in Belgium) giving and receiving information, even though this may be done through a fixed office; but it does include signing of contracts, even though all agreements are subject to confirmation in New York.

And when is it "continuous"? Professor Serick warns that trans-
actions in Germany may result in an "establishment" when they are designed to create an enduring source of income over a long period; this might include negotiations for patent licensing, even though no more transactions will take place in Germany after the initial one.

In summary, we think that a company may safely send its employees to Europe for short visits and even let them sell or buy for it there in transactions having no long-term aspects. It may keep employees indefinitely in Europe to display wares and give technical information and advice on its products. But if it has employees residing in Europe, and if they negotiate contracts, it probably needs to license and register itself (or a subsidiary) as the place where the employees maintain their center of activities.

c. Liability to Taxes on Income and Capital

For tax purposes, the question of what constitutes establishment is governed in five of the six countries of the Common Market by tax treaties with the United States.24 These treaties are very favorable, and take a much more tolerant view of what activities can be carried on without "establishment" than does the commercial law. The one country which has not ratified a U.S. tax treaty is Luxembourg. The failure to ratify the treaty is not generally ascribed to any desire to tax American enterprises but to an unwillingness to exchange with the U.S. Treasury information on tax evaders. Luxembourg’s non-ratification is therefore due to an excess of cordiality to foreign enterprise, rather than to any tax-hunger. It is safe to assume that Luxembourg will not impose taxes in circumstances in which neighboring countries would not.

All the tax treaties contain specific language which preclude the levying of taxes on the enterprise merely because of the presence of agents. The Belgian treaty, which is fairly representative, pro-
provides that a "permanent establishment . . . does not include an agency unless the agent has, and habitually exercises, a general authority to negotiate and conclude contracts on behalf of such enterprise, or has a control over a stock of merchandise from which he regularly fulfills orders on behalf of such enterprise." 25 Thus it appears that an agency may fall short of being an establishment for tax purposes even though it would be deemed an establishment under the laws relating to licensing of foreign enterprises and registration of all commercial businesses.

Purchasing enjoys a special status under the tax treaties with five of the Common Market countries. All these treaties provide that an agency shall not be considered an establishment (for tax purposes) if its activities consist only of purchasing. Of course this clause grants no exemption from the requirements of commercial licensing and registration.

4. THE COMMISSION MERCHANT

The six nations of the E.E.C. possess a well defined commercial institution which is remarkably adapted to the needs of a foreign enterprise which wants to do business in the community. This is the commission merchant or commission agent, known in various European languages as commissionnaire, Kommissionär, commissionario, and commissionnair.

As his name suggests, the commission merchant is normally paid primarily in proportion to the business that he transacts. In addition—and this is perhaps the most important legal characteristic—he does business in his own name. For this reason, he is sometimes compared by legal writers with the American "agent for an undisclosed principal." The comparison is valid, but must not be understood as indicating that the commission merchant is concealing the person for whose account he buys and sells. The important point is that his letters and his invoices bear his own name, not the principal's; and in his dealing with third persons, he says, "I will sell you," not, "My principal will sell you." In addition to these characteristics, the commission merchant is described by European lawyers as one who is in the business of representing several clients and conducting his business according to his own independent ideas, rather than under the direction and control of a single enterprise.

With a European commission merchant an American enterprise

25 Treaty with Belgium art. II(1). The law of Luxembourg, with which the U.S. has no tax treaty, is similar. Einkommensteuergesetz art. 49(2).
can be continuously and conspicuously represented in Europe without incurring any more legal burdens than the firm which sits in New York waiting for Europeans to come and buy. The American enterprise is not liable, under prevailing European legal doctrine, for the contracts which the commission merchant makes (in his own name) on the American concern’s behalf. This is one of the celebrated contrasts between European and Anglo-American law relating to undisclosed principals. A recent essay of Dean Hamel (of the Paris Law Faculty) casts some doubt on the future of this doctrine in France; but in Germany and Italy the rule is firmly entrenched in an express provision of the Civil Code.

For purposes of commercial licensing and registration, it is clear that the commission merchant insulates the principal under European law. The commission merchant must be registered as a merchant, but the principal need not be. Being a local resident, the commission merchant will not need the special license which the foreign enterprise would require; but if any licenses are required, the commission merchant is the one to hold them. For purposes of exchange control the commission merchant is local, the principal foreign.

For tax purposes the status of the commission merchant and his principal are equally clear. Each of the five double-taxation treaties provides specifically that a “bona fide commission agent” shall not constitute an “establishment of the enterprise which employs him.”

There is one important danger in connection with the commission merchant. The employer may wish to switch from one commission merchant to another; or, becoming more deeply interested in the European market, may wish to supplant the commission merchant with a branch or subsidiary which will be under more complete control. Even though the commission merchant has been promised no specific tenure, the interruption of his profitable business, without

---


28 Germany: BGB § 164(2).

Italy: Codice Civile art. 1705. Our Italian collaborator, Mr. Bruna, calls attention to a qualification which may also apply elsewhere. If the undisclosed agent is in charge of a business establishment that belongs to the undisclosed principal, he may be regarded not as a “commission merchant” but as an institore, and may render the principal liable even by a contract in the agent’s name. Codice Civile art. 2208.

Note 24 supra.
good cause or reasonable notice, entitles him to be paid damages equal to his prospective profits.

Fortunately, this danger can generally be excluded by contract; the initial contract may provide for termination of the representation without damages. This provision will be honored in all of the Common Market countries except France. In this respect, a commission merchant differs from a salaried employee, whose right to severance benefits is generally a matter of public policy which cannot be modified by private contract.

5. A BUSINESS OFFICE

Can an American enterprise maintain a business office in Europe, and still contend plausibly that it does not have a European establishment? The general answer must be "no." If there is a fixed place at which business activities are carried on on behalf of an enterprise, this is the very meaning of "establishment" in European law. The office must be licensed as a branch, or incorporated as a subsidiary.

For tax purposes, however, there are some possible exceptions to this generalization. The tax treaties with Belgium, Germany, Italy, and the Netherlands provide that a place of business used exclusively for purchasing shall not be considered an establishment. The tax treaty with France has a slightly different provision with similar effect. In Germany there is no permanent establishment for tax purposes by virtue of activities which persist for less than twelve months.

An interesting question suggests itself in relation to the current activities of various American companies in gathering information on possible investments, or obtaining information on the progress of existing investments. Must the company's representatives do their business from hotel rooms, using always a personal address? Or may they rent an office, hire a secretary, and write "New World Mfg. Co." over the door? We cannot find that this question has been the subject of either legislation or litigation in Europe. Our collaborators incline to the opinion that if the American company's representatives neither make nor receive offers to buy or sell—leaving all such matters for direct correspondence between European prospects and the home office in the States—such an office can be

30 Decree No. 1345 of Dec. 25, 1958, art. 3. Previously, French law recognized the validity of exculpatory clauses.
maintained without fear of involving an "establishment" in commercial or tax law.

6. WITHDRAWING AN ESTABLISHMENT

Today, all eyes are on the opening of establishments. American companies are hurrying to get sites and form business connections with European firms; European officials in many countries are luring foreign investors with cheap real estate, tax concessions, and low-interest loans. These are times for an investor to pinch himself and ask what will be the problems in case the establishment proves unwise and must be withdrawn.

Officers of a well known American factory in one European country told us that they are thinking of moving to another country, but doubt if local officials will "let us." This is a figure of speech, since local officials have no power to force companies to keep operating. But all the ingenuity which they know how to use to induce a company to come in can be very effectively used to deter them from going out. Large amounts of income tax may be found to be due because of understated assets, overstated depreciation, and the realization through sale of previously unrealized appreciation of fixed assets. Friendly assessments of property may suddenly turn hostile; exchange licenses to withdraw the investment may be hard to get. Plant may prove unsaleable because buyers are not assured of permits to make alterations. Conceivably an easier means of withdrawal will eventually be supplied by new uniform laws or treaty provisions covering international mergers. The Member States have promised to "engage in negotiations" looking to this end.31 In the meantime, any withdrawal of an establishment is likely to involve a greater sacrifice of going-concern values than would usually be expected in the United States.

C. SUMMARY ON ESTABLISHMENT

If an enterprise wishes to avoid all European problems, the safest course is, of course, to do no business with Europeans. But it need not be quite so cautious; it may sell to Europeans for payment in the United States without serious involvement in European law. The important line of demarcation is that the enterprise must own no property in Europe and be owed no money by Europeans.

Once the American enterprise has merchandise in Europe, or accounts payable by Europeans, it is potentially concerned with Euro-

31 The Treaty art. 220.
pean law and procedure; it may have to hire a European lawyer to protect its interests. But this need is contingent on running into legal difficulties. If all debtors pay up, and there are no arguments about property, the American enterprise may coast along for years without a thought of European law or litigation.

In this state of potential involvement, without actually feeling any pain, an American enterprise may own goods in Europe, own accounts payable in Europe, license patents, and maintain personnel temporarily or even permanently in Europe so long as they do not buy or sell but perform only technical services.

If, however, the American enterprise decides that it wants to keep people in Europe to sell for it, or solicit sales, during more than short and casual visits, it must make a choice. Either it must "establish" in the countries involved—by branch or subsidiary—or it must choose a registered European commission merchant to represent it. In the former case, the company's European activities become fully subject to European commercial and tax laws; in the latter, they may remain completely immune. Companies which desire only to purchase in Europe—without selling—are more fortunate; in most countries, they can open an office without incurring European tax burdens on their income or capital, although they are required to conform to European commercial licensing and registration provisions.

II. THE FORM OF ESTABLISHMENT

We turn our attention now from the enterprise which is deciding whether or not to create a European establishment to the enterprise which has decided to establish itself on the continent. This it may do in two main ways—by setting up a European branch, or by incorporating a European subsidiary.

The distinction between a branch and a subsidiary is a legal one. To production managers and sales managers it may seem unimportant. We have heard many executives refer to "our Swiss branch," or "our Italian branch," when further investigation reveals that the Swiss or Italian operation is not in legal terms a branch but a subsidiary.

To lawyers, the distinction is fundamental, and its legal consequences are great. A branch of an American company is an establishment whose property is bought and sold in the name of the American corporation; its supreme authority lies in the American board
of directors, and its fundamental constitution is the articles of incorpora­tion first filed in an American state. A European subsidiary is a company whose fundamental constitution was first filed in a European state; it has a name distinct from that of its American parent, and its property is bought and sold in the European name; its supreme authority in law (if not in practice) is exercised by the shareholders of the European company.

The choice between branch and subsidiary presents itself at more than one level. There is first the question whether the American company should maintain European branches, or form European subsidiaries. There is a further question whether one of the European subsidiaries should have branches in various European countries, or whether there should be a separate subsidiary for each country in which the American company wants to conduct business operations. We will take up these questions one at a time.

A. Branch or Subsidiary

In discussions of European trade, it is common to assume without even discussing the matter that any European establishment should take the form of a subsidiary company. We do not challenge the correctness of this assumption in most cases, but there are certainly some situations in which it is inapplicable. For instance, American banks and transportation companies generally operate through branch offices. One of the reasons is economic, not legal; their customers demand the responsibility of the entire enterprise, not of some fraction of it. A legal reason is that the transactions of transferring money or goods or people cannot be severed in mid-Atlantic so as to have a different corporation at each end. These examples are sufficient to show that experienced international organizations do not always choose the subsidiary form. We think that most lawyers will want to determine for themselves whether their enterprises belong in the large class for which subsidiary organization is indicated, or in the smaller group for which branches are appropriate.

I. U.S. Income Taxes

For most American enterprises, subsidiary organization rather than branch has been dictated by U.S. income tax considerations, and may continue to be. However, the tax factors merit re-examination in the light of the characteristics of the particular enterprise, and of possible legislative developments. Legislation which was proposed to the 86th Congress would have gone far to eliminate the
U.S. tax disadvantages of a branch. Although most of the proposed changes were deleted before the bill was passed, the facts that such legislation was proposed and that some remnants of it were enacted suggest that a re-evaluation of branch advantages may be appropriate for many companies.

Even if there are no legislative changes, some kinds of enterprises do not get the same tax advantage from subsidiary organization which others do. One principal advantage is the non-taxability of subsidiary earnings which are allowed to remain in the foreign subsidiary. If all the earnings of the foreign subsidiary are to be immediately repatriated, there is no advantage from this source. Consequently, enterprises which do not plan to reinvest abroad their foreign earnings should consider carefully whether the subsidiary arrangement has merits for them.

Subsidiary organization should be regarded even more dubiously by enterprises which do not intend to earn net income abroad. In this category fall companies which use Europe chiefly as a place to buy supplies (like American watch merchants) or to perform services which have been paid for in the United States (like travel and shipping companies).

2. EUROPEAN TAXES

The American enterprise will also want to consider what differences the choice between branch and subsidiary makes to European taxes. It will be particularly interested in provisions of the double taxation treaties which bind the United States to all of the Common Market countries except Luxembourg. For example, they all provide that American enterprises shall not be taxed on profits other than those allocable to the permanent establishment in the taxing country. They all provide that there shall be no tax at all on the profits of establishments whose only activities are purchasing.

---

33 Cited supra note 24.
34 Treaty with Belgium art. III(1); Treaty with France art. III; Treaty with Germany art. III(1); Treaty with Italy art. III(1); Treaty with the Netherlands art. III(1).
35 Treaty with Belgium art. III(2); Treaty with France art. III; Treaty with Germany art. III(2); Treaty with Italy art. III(2); Treaty with the Netherlands art. II(1), and art. III(2).
They all have an anti-siphoning clause, providing that the taxing country may “rectify the accounts” of the establishment, if it is paying its American affiliate more for goods than would be paid to an unrelated seller.\(^{36}\)

The general effect of these provisions is apparently to eliminate any substantial advantage under European taxes which a subsidiary might have over a branch, or vice versa. However, the apparent effect of such legislative provisions is not always the same as the practical effect. We have heard suggestions from some experienced businessmen that in practice it is easier to agree with European tax assessors on the taxes due from a subsidiary than on those from a branch; the assessors are less likely to “rectify the accounts” of the former than of the latter. Other informants are dubious of this difference, and we are unable to evaluate the respective reports. For an analysis of European taxes on American-owned establishments in Europe, we refer the readers to Chapter XI *infra* by Mr. van Hoorn and Professor Wright.

### 3. Political and Public Relations

Close in importance to taxes are political and public relations. Some of our informants are extremely emphatic about the advantage of operating a “local” company in each country. In France, executives of a large American-owned French subsidiary explained how they must go to government officials for permission to expand the plant, or to make a wage adjustment, or to obtain foreign exchange for materials purchases, or for making a public offering of securities. Even borrowing money from a bank is in France a form of dealing with the government, since most of the banks are state-owned; and the Crédit National, which rediscounts intermediate term loans, is a bank specially formed by the government to promote national economic interests.

All these agencies base their decisions on the national interests of France. Each decision depends on whether, in the officials’ opinions, the company’s activities will benefit the French economy; whether the long term gain outweighs the immediate inflationary effect of increasing construction, increasing wages, spending foreign exchange and expanding credit. Inevitably, the building up of a “French” company appeals more readily to these officials than the building up of an “American” corporation, even though the former is known to be American-owned.

\(^{36}\) Treaty with Belgium art. IV(a); Treaty with France art. IV; Treaty with Germany art. IV; Treaty with Italy art. IV; Treaty with Netherlands art. IV.
Localization also helps to recruit the best types of executive personnel. To be the general manager of a French company gives a sense of prestige and security which cannot be given to the manager of a French branch which is a very small fraction of the American company's entire operation.

These differences between subsidiary organization and branch organization are more marked in some countries than others. Our French and Italian informants have been very emphatic about them; our Belgian and Luxembourg informants give them little weight. We suspect that this disparity of opinion reflects real differences in conditions in the various countries. So far as the differences relate to dealings with government officials, they will obviously vary with the extent of government intervention. France and Italy are countries in which government controls are extremely pervasive; Belgium and Luxembourg are countries with a high degree of economic freedom. France and Italy have had a wall of protective tariffs and exchange controls; Belgium is traditionally free-trading, with a minimum of exchange regulation.

Although comments on national psychology are to be treated with great reserve, we think there are genuine differences in the prevailing attitudes in different European countries toward foreign enterprise. The inhabitants of Benelux recognize without embarrassment the smallness of their economic sphere; association with foreign enterprise gives a sense of security, rather than insecurity. Frenchmen are much slower to accept the idea that a foreign enterprise may offer them something which a domestic enterprise could not.

We therefore accept the view that there are reasons of a psychological character, quite aside from any legal rules, which make a subsidiary preferable to a branch, at least in France and Italy. In the Benelux countries, the psychological factor is of doubtful significance, and the reasons for subsidiary organization (which prevails there as elsewhere) have been chiefly U.S. tax reasons. Our German reports, although less explicit, are more like those from the Benelux countries.

4. COMMERCIAL FILING AND REGISTRATION

All the European countries require filing of the organic documents of a company in the Commercial Register, the Court of Commerce, or some combination of these. Four out of six countries also re-

---

37 Filing of documents:
France: Decree No. 58–1355 of Dec. 27, 1958, [1959] Journal Officiel de la Ré-
quire newspaper publication. In order to be filed the documents must first be translated into the local language. The documents to be filed vary somewhat from country to country. Universally they include the articles of incorporation and any subsequent amendments. In Belgium, Italy, and Luxembourg they also include annual financial statements, statements of profit or loss, and changes in directors and officers, so that re-filing and re-publication must be made at least annually. In France and the Netherlands the larger of the companies which are listed on stock exchanges, and some of their subsidiaries, must publish financial statements.

These requirements apply in rather parallel fashion to branches of foreign companies, and to domestic companies. However, the same filing requirement may be quite different when it is applied to different forms of organization. If the parent company has a long

**Requirements for Filing and Publication**

**Belgium:**
- Articles of Incorporation
- Annual Financial Statements
- Changes in Directors and Officers
- Re-filing and Re-publication

**France:**
- Financial Statements
- Branches of Listed Companies

**Netherlands:**
- Financial Statements
- Branches of Listed Companies

**Luxembourg:**
- Financial Statements
- Branches of Listed Companies

**Germany:**
- Articles of Incorporation
- Financial Statements
- Names and Signatures of Managers

**Italy:**
- Articles of Incorporation
- Financial Statements
- Names and Signatures of Managers

**Netherlands:**
- Name and Address of Company
- Personal Details on Officers

**Luxembourg:**
- Articles of Incorporation
- Financial Statements

**France:**
- Articles of Incorporation
- Financial Statements

**Germany:**
- Articles of Incorporation
- Financial Statements

**Italy:**
- Articles of Incorporation
- Financial Statements

**Netherlands:**
- Articles of Incorporation
- Financial Statements

**Luxembourg:**
- Articles of Incorporation
- Financial Statements

**France:**
- Articles of Incorporation
- Financial Statements

**Germany:**
- Articles of Incorporation
- Financial Statements

**Italy:**
- Articles of Incorporation
- Financial Statements

**Netherlands:**
- Articles of Incorporation
- Financial Statements

**Luxembourg:**
- Articles of Incorporation
- Financial Statements

**France:**
- Articles of Incorporation
- Financial Statements

**Germany:**
- Articles of Incorporation
- Financial Statements

**Italy:**
- Articles of Incorporation
- Financial Statements

**Netherlands:**
- Articles of Incorporation
- Financial Statements

**Luxembourg:**
- Articles of Incorporation
- Financial Statements

---

**Publication Requirements:**

**Belgium:**
- Names, Professions, and Addresses of Members of Governing Boards and Auditors

**France:**
- Extract of Articles

**Germany:**
- Commercial Register Entries

**Luxembourg:**
- Articles and Financial Statements

**France:**
- Commercial Register Entries

**Netherlands:**
- Name and Address of Company

**Luxembourg:**
- Articles and Financial Statements

---

**Repetition:**

**Belgium:**
- Articles of Incorporation

**Italy:**
- Articles of Incorporation

**Luxembourg:**
- Articles of Incorporation

---

**France:**

**Netherlands:**
- W.K. art. 42 c.

**Italy:**
- Amendments of Charter

---

**Notes:**

1. France is an exception. Amendments of charter need not be filed, nor changes in officers other than managers of the Italian branches.
charter, the burden of translating and filing it may be considerably greater than that of forming a subsidiary and filing its charter; the burden is perhaps more likely to be felt with respect to filing amendments in the country of each establishment. When the Chase National Bank merged with the Bank of Manhattan, new articles of incorporation had to be filed in Paris because of the Paris branch. If the Paris establishment had been a subsidiary (which is not practicable in the case of a bank), no such filing would have been necessary.

Similar considerations may apply to publication of financial statements where, as in Belgium, they are required. Branches and subsidiaries are subject to the same requirement, but the branch must publish the statements of the whole company to which it belongs while the subsidiary needs to publish only its separate statement.

5. THE FOREIGN MERCHANT'S IDENTITY CARD

In addition to registering the establishment, the laws of Belgium and France require a permit for the general manager or president, if he is a foreigner. This executive must have a "foreign merchant's identity card" (*carte d'identité de commerçant étranger*). In France the card is issued after the prefect has been satisfied that the proposed commercial activity is useful to the economy and that the applicant has a good business record. The prefect satisfies himself on the former point by consulting the trade associations of the industry in which the applicant intends to be active. This might seem to give the local merchants a veto on new competition; presumably it does, as far as concerns businessmen like brokers, who pursue their occupations as individuals. As to corporations, the competitors have the power only to force the company to have a local president, by rejecting the foreign one; the foreigner who is rejected as president may serve instead as technical director. Therefore the foreign merchant's card is not likely to be denied on economic grounds. The "good business record" of the applicant is commonly determined by statements from chambers of commerce.

The practical difficulty presented by the foreign merchant's card is only a matter of delay. Several months may elapse between application and issue, but eventual denial has not been, we are told, a frequent problem for Americans.

In Belgium, the foreign merchant's card is harder to come by; in practice, foreign concerns find it best to appoint Belgians as chief executives of their Belgian branches and subsidiaries.
In both countries, the "foreign merchant's card" is the same problem for a branch as it is for a subsidiary.

6. LIABILITY FOR OBLIGATIONS OF BRANCHES AND SUBSIDIARIES

In any vast commercial network, the responsibilities of one sector of the network for the obligations of other sectors present a complex problem. We would like to divide the problem into two main parts. The first part of the problem arises when the sector in which the obligations were incurred becomes insolvent, and cannot pay its debts; the question arises whether the other sectors can be made to pay. We will call this the insolvency problem.

The second problem is quite different. We assume that the sector in which the obligations were incurred is quite able to pay them, but for some reason the plaintiff elects to bring his suit in some other sector. A classic American illustration of this problem is the case in which an individual was injured by a street car in the Philippine Islands, and elected to sue the parent company, which owned the street car operating company, at the parent company's home in Connecticut; one can imagine similar suits arising from subsidiaries in Europe. Suits of this sort have acquired in the United States the name of "migratory suits," and we will therefore refer in this connection to the migratory suit problem.

We do not think the insolvency problem will loom large in the plans of American enterprise; they will plan to pay the debts which their subsidiaries incur. But it is a hazard which merits some attention even though it is marginal.

a. The Insolvency Problem: Branch Organization

If a European branch of an American corporation proves unable to pay its debts, there is no doubt of the European creditors' right to sue the corporation in the United States, or wherever else it might be found. It is a single legal person, regardless of the number of its branches. If the suit had been first brought to judgment in Europe, any court in the United States would recognize its validity, since the establishment of a European branch would give the European court "jurisdiction" by American standards. If the cause of action had never been sued on in Europe, an original suit on it could be begun in the United States.

b. The Insolvency Problem: Subsidiary Organization

If an American corporation forms subsidiaries in Europe, rather than branches, a very different problem is presented. In Europe, as in America, different corporations are different persons. The fact that one owns stock in another is not enough to make both liable for the same debt.

But sometimes stock ownership is not the whole story of the corporate relationship. There may be 100% ownership, or near it; there may be intermingled management and intermingled property; there may be such inadequate capitalization that insolvency should have been foreseen; there may even have been an intention to incur obligations which would never be discharged. Which, if any, of these circumstances will lead to a judgment that the American parent is liable for the European subsidiary’s debts?

A preliminary question, in considering this problem, is what law would govern. Since the European subsidiary is by hypothesis insolvent, the liability of the parent would most likely be litigated in an American federal court. If so, a federal court would decide which legal regime to apply. But the events which would determine the legal regime would almost inevitably be distributed between two continents, and a plausible ground could be found for applying the law either of the European country most involved, or of the United States.

Readers are already familiar with American judicial reactions to the question of when a parent corporation should be made to pay the debts of an insolvent subsidiary. They know that American courts—especially federal courts—have held shareholders and affiliated corporations liable for debts contracted by a company which is formed largely to acquire assets for its owners, but which has no substantial independent existence, whether measured in terms of capital investment or of management structure. The court disregards “the entity,” or “the fiction”; it “pierces” or “draws aside” the corporate veil.

Germany has experienced a very similar development of legal theory, in which Durchgriff der juristischen Persone, [piercing the artificial person] and Missachtung der Rechtsform [disregard of
legal form] take the place of the American magic words. Some of the factors which have been determinative in American cases are also influential in German cases; the mingling of personal and company assets is most prominent, but inadequate capitalization is also recognized. We cannot say whether German courts are generally more or less disposed to "pierce the veil"; the comparatists' observation that American case-law is far more developed on this subject suggests that our courts may be more disposed to "pierce."

In France, we encounter no theory of "piercing" or "disregard," but the same effects are achieved, and with a vengeance. The doctrinal basis is called "abuse of entity" [abus de la personnalité], the idea being that the establishment of a corporation may be a mere pretense, designed to exploit unfairly (that is, to "abuse") the privilege of limited liability. When the courts detect the abuse, they search for the real principal (the commerçant de fait), and hold him liable. This principle, which grew out of case law, is now a clause in the French bankruptcy act, which provides,

When a company is declared bankrupt, the bankruptcy may be declared to include any other person who, disguising his acts as those of the company, has carried on business for his personal benefit, and has dealt with the corporate assets as though they were his own.

Professor Houin offers the following comment on the application of this rule:

If the subsidiary is a mere department of the parent company, if the majority of its shares are held by the parent company or its shareholders, if the governing board members are the same, if the accounting is more or less intermingled, if personnel pass freely from one company to the other,—then the court will say that the two companies are really only one entity and one fund; their debts are the same, and so the bankruptcy of either brings in its train the bankruptcy of the other.

43 SERICK, REICHTSFORM UND REALITÄT JURISTISCHER PERSONEN, (Beiträge zum Ausländischen und Internationalen Privatrecht, No. 26, 1955); SERICK, DURCHGRiffS­PROBLEME BEI VERTRAGSSTÖRUNGEN (Juristische Studiengesellschaft Karlsruhe, No. 42, 1959); DROBNIG, HAFTUNGSDURCHGRiff BEI KAPITALGESELLSCHAFTEN, (Arbeiten zur Rechtsvergleichung, No. 4, 1959).
44 DROBNIG, op. cit., supra note 43, at 28, 47.
45 Id. at 25; cf. SERICK, REICHTSFORM UND REALITÄT JURISTISCHER PERSONEN 65, 66.
46 Decree No. 55-583 of May 20, 1955, art. 10, [1955] JOURNAL OFFICIEL DE LA Ré­PUBLIQUE FRANçAISE 5086. Identical provisions were formerly part of C. Com. art. 437, as amended by a decree-law of 1935.
Thus it appears that French and German courts are not unlikely to impose liability on parent companies (to the extent that parent companies are within their power) when subservient subsidiaries become bankrupt. A subsidiary will not be a good "insulator" against debts in those countries, unless it can be shown to be truly independent (within the varying standards of independence).

In the other countries of Europe, the imposition of liability on these grounds is not yet a known peril. Our Belgian, Luxembourg, and Netherlands collaborators report that the "abuse of entity" and "disregard of entity" doctrines have not yet been used in their countries, although analogous effects may be attained in relation to enemy property.

However, parent corporations may easily incur liability in Italy or in France because of failure to have the necessary number of shareholders. The Italian code declares that a sole owner is liable for debts contracted during his sole ownership.\(^{46a}\) In France, one hundred percent ownership of a subsidiary’s stock would probably make the parent liable for all the subsidiary’s obligations on the theory that the subsidiary cannot be a "company" if it has only one member.

c. The Migratory Suit Problem: Branch Organization

The migratory suit problem, unlike the insolvency problem, is one which may disturb an American company even though it is determined to pay all the just debts incurred in its operations. In fact, the sounder the company, the more likely a victim it is for the migratory suitor. This is the danger that a plaintiff with a cause of action which arose in Honolulu will choose to sue in Frankfurt or Paris.

The company's objection to such suits is not that it does not want to pay Honolulu plaintiffs, but that it does not like to litigate with them at a distance of several thousand miles from all the witnesses and the documents.

This hazard may be viewed in two forms. One is the danger that the European branches will be the victims of suits arising in the United States (or in other continents where branches may be found); the other danger is that European branches will give rise to suits which may be prosecuted in the United States (or other continents).

\(^{46a}\) C. Civ. 2362 (stock companies). Experts disagree on the effectiveness of dummy "shareholders" in fulfilling the legal requirement.
Taking first the problem of suits brought in Europe, it appears to us that there is no legal defense against such suits. If the defendant resides within the court's area, the court has jurisdiction, regardless of the place of origin of the cause of action; and establishment of a branch is regarded as equivalent to residence. European courts do not seem to apply the doctrine of *forum non conveniens*.

On the other hand, we have not encountered any American company which has experienced serious inconvenience from this source. Three peculiarities of European practice offer possible explanations. One is that the contingent lawyer's fee is unknown in Europe; probably most of the migratory suits in the United States are filed by lawyers on contingent fees. A second reason is that in European procedure, the parties are not allowed to testify. Therefore a Honolulu plaintiff cannot transport his law-suit to Paris merely by transporting himself; he must bring witnesses, too; and this makes the suit just as inconvenient for him as it is for the defendant. Third, the plaintiff must pay the defendant's counsel fees if he fails to win his case, and the foreign plaintiff must deposit security in advance to assure this payment.

We take up next the problem of suits originating in Europe but prosecuted in the United States. For instance, a European might be injured by a defective machine manufactured by an American corporation's German branch, and might sue in New York. Conceivably the court might refuse jurisdiction on the ground of *forum non conveniens*; otherwise the suit would lie. If the injured plaintiff were one of the hundreds of thousands of Americans who tour Europe each summer, the plea would probably be rejected. Thus branch organization increases a company's exposure to migratory suits.

In practice, this problem has not been an acute one for American companies; but we do not find any explanation except that the branch form of organization has been very little used. We are inclined to think that migratory suits are a real danger for companies whose activities may occasion personal injuries. It is a valid reason for avoiding branch organization.

d. The Migratory Suit Problem: Subsidiary Organization

If an American company operates in Europe only through subsidiaries, it appears to be relatively safe from migratory suits in Europe. The European subsidiaries are different legal persons from the parent, and there seems to be no danger that any of the Euro-
pean doctrines would support the suit. These doctrines have sometimes visited the sins of the subsidiaries upon the parents, but never vice versa.

A suit against the parent in the United States presents no great dangers, either. If we look to the relevant European doctrines, we find that they have never held the parent liable except when the subsidiary has proved insolvent or has only one shareholder; the migratory suit problem has not appeared. Thus the only danger lies in the application of United States doctrines on disregard of corporate entity. Without fully exploring this engaging topic, we may say that if the parent rigorously separates the operations of the subsidiary from its own, and the subsidiary avoids insolvency, danger should be avoided.

7. CHANGE OF FORM: INCORPORATING A BRANCH

In the United States, the choice between a branch and a subsidiary form is far from irrevocable. If a branch is opened, but subsidiary organization later appears preferable, the branch may be incorporated without serious tax consequences; the exchange of stock for proprietorship is not regarded as a realization of taxable income. Further, the taxes incurred by transferring the assets (for example the documentary stamp tax on the deed of real estate) are negligible.

In Europe, the opposite is true. The transfer of assets to a new corporation in exchange for stock is regarded as a realization of income. If the stock is worth more than the incorporators' basis for the assets, augmented by any retained earnings on which income taxes have been paid, income is realized. European accounting commonly employs "hidden reserves" which understate annual income. This practice, although perhaps improper, is so generally followed that tax writers take for granted the appearance on liquidation of previously unreported earnings. As a result of the practice, a very large amount of income tax which had been postponed becomes payable when a branch is incorporated, as well as when a subsidiary is dissolved.

There are also taxes in some European countries on the transfer of all kinds of assets to a company in exchange for stock. The Belgian rate, for instance, is 1.6%. The combined effect of these taxes and the income taxes is to discourage formation of a branch with the intention of later incorporating it as a separate subsidiary.

The deterrents to forming a subsidiary with the intention of turn-
ing it later into a branch are even greater. The dissolution of a subsidiary generally results in a “sale” of the fixed assets, incurring taxes reported as 8% in Italy, 11% in Belgium, and 15% in France of the value of the assets. Rates on transfer of the inventory are lower—about 4 or 5%. There are sometimes means of effecting a tax-free merger, but such avenues of escape are the exception rather than the rule in Europe.

8. CLOSING OUT THE OPERATION

We have spoken so far of the relative advantages of a branch or of a subsidiary in carrying on operations. But the investor must also give some attention to their relative advantages in closing out operations; that is, disposing of it to outsiders. If the operation proves unprofitable, it will have to be closed out. Even if it proves successful, the operation in a neighboring country may be so much more successful that the investor will want to liquidate his German establishment (for instance) in order to concentrate his operations in France. The formation of the Community has already produced some such results, while the projected changes in tariffs and quotas are still in their infancy.

One way to close out is to sell the assets for cash. This results in the same taxes already discussed in relation to a change of form from branch to subsidiary, or vice versa. There is a tax on previously unrealized or unreported income, and transfer taxes on the assets. The burden is the same for a branch as for a subsidiary.

Another way is to sell the shares owned in the European enterprise. This involves no tax at all, or taxes in very small amounts; for instance, in Germany, less than one-fourth of one percent of the par value of the shares.

Obviously the sale of shares is much more advantageous, at least to the seller. But this option is available only if the European operation has been cast in a subsidiary form; one cannot sell shares in a branch. This is one of many reasons why a subsidiary is so widely preferred for European operations.

A third way to dispose of a European operation, which would suggest itself to an American tax or corporation lawyer, is to merge it with some outside company that wants to buy it. That is, the American subsidiary could be merged with some other European corporation which wished to acquire the assets. Our information on this point is incomplete, but it appears that a merger normally has
no tax advantages over a sale of assets. Heavy taxes on income and on transfer of property are usually incurred.

There are limited exceptions to this rule. A merger between two Luxembourg companies which maintain adequate accounting records is entirely tax-free. In Belgium, there is a temporary exception, available to Belgian companies which merge during the "first stage" of the European Economic Community—that is, before the end of 1961. It is limited to mergers which "contribute to economic rationalization, higher productivity, or greater employment." France permits some taxes to be escaped in restricted types of mergers. There have been press reports of similar legislation in Italy. It is possible that further tax concessions to merger will result from the negotiations which the Member States have agreed to undertake with regard to international merger.

Where merger has these advantages, they are advantages only for those investors who have put their investment in subsidiary form: there is no way to merge a branch.

9. SUMMARY ON BRANCHES OR SUBSIDIARIES

For a few enterprises—chiefly banks—the choice of a branch rather than a subsidiary is clearly dictated by the economic needs of the business. For most enterprises, either form is equally functional, and the choice will be dictated by other factors. Among these, U.S. income taxation is likely to prove dominant, and to favor subsidiary organization; but it will have less significance for some types of enterprise—notably purchasing organizations. European taxes on current income are neutral for most enterprises, while the establishment continues; but if the American investor finds it necessary to dispose of his European venture, a subsidiary is likely to offer a much more economical means of getting out. Political relationships will dictate subsidiary organization for many enterprises, especially those which encounter pervasive state regulation. Public filing and registration rules seem fairly neutral, but favor the subsidiary in some cases. If there is a desire to avoid becoming involved in the debts which may be incurred by the foreign operation, subsidiary operation is clearly indicated; but it may fail in its purpose unless the subsidiary is truly independent in its financing and man-

47 Loi sur l'impôt sur les collectivités (Körperschaftsteuergesetz) art. 15.
48 Law of July 15, 1959, as reported by Belgian Industrial Information Service, August 1959, p. 1.
49 The Treaty art. 41.
agement. Where the migratory law suit is a problem, subsidiary organization is clearly preferable.

In conclusion, subsidiary organization offers substantial advantages in a majority of situations, but not in all. The factors which have been listed above may prove helpful in making the choice for a particular venture.

B. How Many Subsidiaries?

We leave behind us now the problems of those enterprises which will operate in Europe by means of branch offices of the American company; we turn to the problems of those who have decided to conduct their operations in Europe through one or more subsidiaries. The next question is, how many subsidiaries? There are six sovereign nations in the Common Market; does an American enterprise need a separate subsidiary for each country in which it has decided to create an establishment? Or may it, for example, form a subsidiary in Belgium which can operate as a single European company in Luxembourg, Netherlands, France, Germany, and Italy? In the following pages we will discuss the possibility of such a Belgian company, as an illustration of the problems which would be met by a single European company established in any one of the Common Market countries, and operating through branches in the others.

The question which we ask is somewhat like the one we have already asked about a U.S. company with branches in Europe. Foreign branches of a Belgian company present many of the same problems presented by foreign branches of a U.S. company. But the problems are not quite the same, and we think the question of branches versus subsidiaries should be re-examined with the hypothesis of a European home office. This we will do, with our Belgian illustration.

I. ADVANTAGES OF A SINGLE EUROPEAN COMPANY

The potential advantages of having a single European company are obviously great. Geography alone demands that an enterprise be able to fill its orders indiscriminately from warehouses in Amsterdam or Aachen, Milan or Marseilles. The enterprise needs to be able to use the same executives and technicians in Liège as in Verdun.

These advantages will appeal particularly to American businessmen, who are accustomed to plan their operations on a continental scale. Indeed, experience in this sort of operation is one of the prin-
principal advantages which Americans may hope to bring to the European market, where they are in most other respects less experienced than local businessmen. Attaining these advantages is one of the very reasons for which the Common Market has been formed; if they cannot be realized, the Market may be an illusion and a disappointment to many of the American enterprises which plan to enter it.

To be sure, it is possible to operate a single enterprise through a half dozen corporations which are separate only in form. But empty forms are expensive at best, and they lead to more serious problems, to which we will refer later.

2. THE PROSPECTIVE EVOLUTION OF THE COMMUNITY

A further impetus toward the single European company may be found in the planned evolution of the European Economic Community under the Treaty of Rome. All of its provisions are designed to make of Western Europe an area without barriers, and in which, therefore, a single company can operate. Article 52 declares that

restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be progressively abolished in the course of the transitional period. Such progressive abolition shall also extend to restrictions on the setting up of agencies, branches or subsidiaries by the nationals of any Member State established in the territory of any Member State.

Many intra-Market impediments are to be substantially abolished within the transitory period which should terminate in 1970 (with possible extensions). In addition to restrictions on freedom of establishment, these include tariffs (Article 13), quotas (Article 30), and obstacles to movement of workers (Article 48), and the supply of services (Article 59). In addition the members have promised to coordinate their exchange controls (Article 70) and to "approximate" any other laws which directly affect the workings of the market (Article 100).

Moreover, the reduction of these obstacles is expected to begin well before 1970. In the first few years rapid progress is likely to be impeded by the requirements of unanimous agreement (establishment, Article 54; diplomas and certificates, Article 57; services, Article 63; capital movements, Article 67). But directives by majority action of the council may be issued even in the first stage (1958–1961) with regard to movement of workers; and in the sec-
ond stage (1962–1965) with regard to establishment, diplomas or certificates, services and laws which distort competition. Restrictions on capital movements are subjected to majority rule in the third stage (1966–1969).

3. OBSTACLES TO A SINGLE EUROPEAN COMPANY

While the attractions of a single European company are great, and will become greater as the Economic Community evolves, the practical lawyer cannot overlook the obstacles which exist today, some of which may continue to exist for a long time. We have already had occasion to examine the principal obstacles to use of European branches of an American company in Europe; we must look to see whether the same obstacles oppose themselves to the use of branches of a Belgian company (for instance) in other European countries.

We may start with taxation. This was found to be a principal obstacle to the operation of branch operation by an American corporation, and may prove to impede operation of branches by European companies too. Without analyzing the tax structures of the various Community countries, which are the subject of a separate study by Messrs. van Hoorn and Wright, we can say that some discrepancies and overlaps are to be expected, and that they are not necessarily eliminated by the "double taxation" treaties existing among several of the Common Market countries, nor by the provisions of the Treaty of Rome. Specific mention of taxation is found only in Articles 95–99 and 220. Articles 95–99 contain strong provisions, but they apply only to "turnover" and similar taxes on goods. Article 220 is much broader; it refers to "elimination of double taxation," with presumed reference to income taxes. But it does not even give directive powers to the Community Council. It merely pledges Member States to "engage in negotiations."

A third possible avenue of attack on tax obstacles to Community-wide operation may be found in Articles 100 and 101. Article 100 empowers the Council to issue directives with respect to "such legislative and administrative provisions as have a direct incidence on the establishment or functioning of the Common Market." Article 101 gives a directive power over provisions which "distort the conditions of competition in the Common Market, and thereby cause a state of affairs which must be eliminated."

Tax deterrents to Community-wide corporate organization would seem to be "indirect" rather than "direct" impediments to the
Market; if they impede progress in all countries equally, they can hardly be said to "distort" competition, although they may retard it a good deal. Thus we would not hold high hopes for the elimination of tax barriers which may presently enforce a policy of separate subsidiaries in separate countries.

A second reason mentioned for setting up subsidiaries rather than branches of the American corporation was to obtain a sympathetic approach from government officials who may pass on the application of an enterprise for a license to build a new plant, to adjust wage rates, to exchange foreign currency, to obtain an import quota allocation, to make a public securities offering. These matters will continue for the foreseeable future to be administered by national, not by international officials. The Community will affect this problem only insofar as the Community reduces the need for dealing with government agencies (by increasing economic freedom), and insofar as the Community diminishes the nationalism of national officials. It may indeed have such effects, but they will be indirect, and may be long delayed.

A final reason for preferring a European subsidiary, rather than a European branch, of an American company was the desire to be insulated from migratory suits, and from debts in case of insolvency of the European enterprise. Both of these objectives are satisfied as well by having one European subsidiary as by having six. As to migratory suits, migration within Europe—for instance from Rome to Brussels—has never been a problem. As to insolvency, the features of inadequate capitalization and domination of subsidiary affairs, which inspire the "piercing of the veil," are more likely to appear in a number of small national subsidiaries than in a larger market-wide subsidiary.

In summary, there are no strong legal obstacles to establishing a single European subsidiary with branches in the other countries. By 1970, this course may be clearly indicated. But in the meantime there are likely to be many inconveniences—difficulties with taxes and with all sorts of administrative regulations—which a single European subsidiary will feel more sharply than separate national subsidiaries would.

4. HARMONIZING SUBSIDIARY OPERATIONS

One special problem of operating through multiple subsidiaries is the necessity of harmonizing their policies to achieve the practical benefits of unified operation. American lawyers are, of course, fa-
miliar with means of operating subsidiaries as if they were mere departments of the parent company. In American practice, the parent company holds all the stock of all the subsidiaries, and the parent’s board frequently makes all major decisions for subsidiary companies; the boards of the various subsidiaries carry out these decisions. But several complications will be encountered in applying this pattern in the Common Market.

On the purely technical plane, there is the rule against the sole ownership of any company’s stock by a single individual or company. This can be solved without much difficulty by issuing single shares to chosen persons who will make up the necessary complement of two, five, or seven shareholders.

A more serious problem is involved in getting the most out of the local directors. The parent company needs keen and devoted local directors in each subsidiary, to solve distinctive local problems. Normally it will install such directors, and award them salaries from the subsidiary’s treasury, plus bonuses based on the subsidiary’s profits. They may be expected to devote themselves to the building up of their company.

Unfortunately, the devotion of this group of local directors is likely to collide with the objectives of the European operation seen as a whole. It may become advantageous to transfer operations from the French subsidiary (for instance) to the Italian subsidiary. The change may cut the bonuses and imperil the salaries of the French directors. Under these conditions, or the threat of these conditions, it may be difficult to attract and hold French directors; or they may lose the initiative and the sense of responsibility which would have resulted from a truly independent French operation.

An ingenious solution to this problem has been suggested. The American parent needs a European policy board, to which the top executives of all the subsidiaries will belong. Part of their bonuses might be based on profits of the subsidiaries as a group, rather than solely on those of their own national subsidiaries. At the least, they should meet together, and acquire a Common Market perspective, and they should be made to feel that their futures depend not only on the success of their national segment of the enterprise, but on the success of the whole. This feeling can be given reality by moving executives from one subsidiary to another. Language differences will impose some limits on this shifting, but it will not be hard to find French-speaking Italians who can work in France, Belgium, or Lux-
embourg and German-speaking Dutchmen or Luxembourgers who can work in Germany.

A European policy board will do more than develop European thinking for the parent company. Western Europe now has a twelve year plan for the evolution of its commercial institutions and its economic life. If advantage is to be taken of the burgeoning opportunities which present themselves, there must be continuous thinking about European operations by people who are close to them; decisions cannot be left for peripheral attention by an American board.

Various legal structures for the European board may be imagined. There might simply be meetings among the directors of the various European subsidiaries; this arrangement would probably fail to supply the needed authority and cohesion. An outstanding solution which has come to our attention is the one announced in the summer of 1958 by the Ford Motor Company, which opened a European office of its International Division. Such a branch would not need to buy or sell, and could therefore escape all the legal effects of "establishment"; at the same time, it could furnish a center of harmonization, and a pole of loyalty.

Whatever structure is adopted, one peril of harmonization must be noticed. It may involve violation of European laws on "restraint of trade." Article 85 of the Treaty of Rome prohibits agreements which result in "(a) the direct or indirect fixing of purchase or selling prices or of any other trading conditions; (b) the limitation or control of production, markets, technical development or investment; [or] (c) market-sharing or the sharing of sources of supply." These provisions purport to be self-operating but will have to be enforced by Member States until implemented by action of the Council.

What should be expected from these provisions is not yet known; another chapter of this book, by Professor Riesenfeld, discusses the problem. Obviously there is some possibility that the harmonization of subsidiaries' policies may run afoul of the Common Market's "antitrust" laws. If this should occur, an enterprise might be better off operating as a single company with branches; a single company cannot make an illegal "agreement" with itself.

A single European company might also violate the competition rules of the Treaty. Under Article 86, a single enterprise with a dominant position in the Common Market is forbidden to limit "production, markets or technical developments to the prejudice of
40 AMERICAN ENTERPRISE IN THE COMMON MARKET

consumers." But this article does not outlaw a single company's market-wide price policy, or marketing plan, as Article 85 outlaws them for a combination of different companies.

5. A EUROPEAN HOLDING COMPANY

Many writers in the past year or two have advocated the formation by an American enterprise of a European holding company to possess the enterprise's shares in foreign operating companies in European countries.

One function of such a holding company is to serve as coordinating agency for the policies of the various operating subsidiaries. But this can be done by establishing a European policy board without the added complication of a holding company.

A second function of some European holding companies has been to conceal the identity or nationality of the investor. This factor has been of great importance in a continent which has been twice in the last half-century tormented by wars, and parts of which have suffered political or racial purges. But concealment is quite impossible for most of the investors whose problems are considered in this paper—that is, American manufacturers who want to exploit in Europe their well known products, processes, or trademarks.

This leaves as the principal function of a European holding company the supplying of a financial conduit, through which the profits of one European subsidiary can be passed to another without passing through any U.S. company. For if the profits pass through an American company, they emerge minus taxes. Such a conduit will be of special interest in the Common Market, because of the possibility that operations now conducted in several of the Market countries may later be concentrated in one of them.

However, a holding company is not the only conceivable means of passing funds from one company to another. Where all the operating subsidiaries are wholly owned, the funds can perhaps just as well be loaned from one to the other. The need of a holding company for European subsidiaries is likely to arise chiefly when the European nationals hold a substantial minority, or a majority, of the company in which the American enterprise has invested. In such cases, the European shareholders will not share the Americans' enthusiasm for transferring the company's resources to an affiliated company in another country.

Three European countries have been widely mentioned as sites for European holding companies—Switzerland, Liechtenstein, and
Luxembourg. We are advised that arrangements can be made with the Netherlands government to exempt from tax income received from subsidiaries in other countries, although there is no express statutory exemption.

Although all these four countries may serve equally well as tax havens, they are not likely to serve equally well as profit conduits, because of differences in their positions with regard to exchange restrictions. If European currencies become soft again, there will be a tendency for countries to protect themselves by restricting withdrawals, or restricting the terms on which new investments may be made. Within the Common Market, the countries have committed themselves to maintaining a high degree of liberality, and their restrictive measures can be reviewed and overruled by the Community Council. The commitments on exchange control between Switzerland and the Common Market countries are much less effective. Hence a holding company located in Luxembourg or Netherlands has a probability of being able to invest and disinvest in other Common Market countries with a good deal more assurance than a holding company in Switzerland or Liechtenstein.

6. MERGING SUBSIDIARIES

The momentary advantages in having several subsidiaries within the Market, and the prospective later advantages of having a single Common Market subsidiary suggest to an American that subsidiaries should be formed now and merged later with other European companies. There are many obstacles to this course, and it should not be planned.

Merger between companies of different countries is presently impracticable. One cannot merge a French company with a German one as he can merge a Delaware corporation with a Pennsylvania one. There are some prospects for future legislation which will permit international mergers; this is one of the subjects on which the Community members promise to "engage in negotiations." But one cannot be certain of it.

51 See Chapter XI infra.
52 Treaty, arts. 67-73. By its first directive under this article, the Council has ordered all member states to grant a general licenses for purchases of securities traded on the stock exchanges of member states, and to grant all licenses that may be required to permit direct investment, and offerings of new securities, among member states. See Directive No. 1 under Article 67, May 11, 1960.
53 The Treaty, art. 220.
There are also some temporary exemptions from the income taxes which would normally be incurred on merger, in order to permit companies to adjust themselves to the Common Market. But these exemptions are not sure to persist to the time when merger may be desired, and when international agreements may have made it possible.

7. SUGGESTED CONCLUSIONS

We have offered a host of considerations for examination in the light of the circumstances of each individual enterprise. What conclusions should be drawn? We will offer a few.

In the Benelux group of three countries, a single company operating across national lines is already practical. For some years General Motors has been operating a Belgian company (General Motors Continental) with a branch factory in Netherlands; their officers report complete satisfaction with the arrangement. They feel that Dutch officials give their branch just as favorable treatment as could have been expected for a purely Dutch company. Most companies appear to be still operating with separate subsidiaries in these nations (Ford Motor has separate subsidiaries for its Dutch and Belgian plants), but we discovered no opinion that this offers any great advantage today.

Outside of Benelux, we know of no instance of international branch operation of factories, although there are many branch banks, transportation offices, and purchasing agencies. We are prepared to accept the conclusion reached by most enterprises that the time has not yet come when it is most convenient to operate an Italian or German factory as a branch of a Belgian company.

On the other hand, we think that the time will come, and very probably within the transitional period of the Common Market. It may be accelerated not only by the abolition of restrictions and by the harmonization of laws, but also by "antitrust" laws which impede the harmonization of policies of separate companies.

The one thing certain is that the best form of organization today may not be the best form tomorrow. This means that in deciding to establish in any country the cost estimates should include the expenses of a probable reorganization within a few years. If the combined costs are too high, the decision should be to defer establishment in the countries where it can most practicably be dispensed with. The market in those countries may be exploited through the use of commission agents, or merely by exports from a foreign base.
We will hazard one more opinion. As the Common Market evolves, conditions will become progressively more favorable to operations of a single European company, and less favorable to operations of a number of European subsidiaries. If the choice between one subsidiary and many is a close decision under today's condition, the single subsidiary should be favored; the future is more likely to increase than to decrease its advantage.

III. FORMING A EUROPEAN SUBSIDIARY

A. THE EUROPEAN COMPANY LAWS

I. FAMILY RESEMBLANCES (AND DIVERGENCIES)

When we make the decision to form a European company, we find ourselves face to face with the European company laws. For the six countries of the Community, there are six systems of company law—all different. And there are not six, but eight sets of legal texts, since two of the countries present their laws in two official languages (Belgium in French and Flemish; Luxembourg in French and German).

That is taking the worst possible view of the matter. On the brighter side, we may notice that four languages cover all eight of the legal texts (French, German, Italian, and Dutch). Furthermore, a knowledge of the French language will permit the reader to examine official texts of three countries (France, Belgium, and Luxembourg), and to examine the translated texts, with latest amendments, of the other three nations. Texts of the relevant laws of all six countries will probably soon be available in German, also.

Moreover, all of the six company law systems reveal strong mutual resemblances, as seen from an American perspective. One discovers again and again concepts which are common to the six countries but unfamiliar in any of the fifty American states. All of the legal systems share basic concepts which were enunciated in the

\[54\] A Paris publisher, Editions Jupiter, prints a loose-leaf service containing the company laws of the six countries, together with analysis and practical suggestions, under the title *RECUEILS PRATIQUES DU DROIT DES AFFAIRES DANS LES PAYS DU MARCHE COMMUN*. (Hereinafter Rec. Prat. du M.C.) In this collection everything not originally in French is translated into that language; Italian and German legal texts in their original languages are also included.

\[55\] The publishers of the Rec. Prat. du M.C. have advised us that they will shortly issue a German language edition. German language translations of company laws of foreign countries are also published by the Gesellschaft für Rechtsvergleichung at Frankfurt, Germany.
Napoleonic Civil and Commercial Codes.\textsuperscript{58} The company laws of Luxembourg, Belgium and Italy also reflect a strong influence of the French Company Law of 1867, which is still in effect in France although considerably amended. German company law contains more radical differences from the French pattern, reflecting in part its independent historical development. While all the European company laws will strike an American lawyer as rather rigid, perhaps even old-fashioned, he will come closest in the Netherlands to discovering the liberty of organization and finance to which he may have been accustomed within the hospital boundaries of Delaware.

Some day, perhaps, there will be uniform company laws throughout the Common Market. A committee in France, and perhaps others elsewhere, are studying the possibility. But the Common Market members are not committed, even in theory, to uniformity in this area. So the six regimes of company law are likely to be with us for some years to come.

2. WHERE TO FIND THE LAWS

Few of the European company laws can conveniently be studied in English.\textsuperscript{58a} Most of the English translations which have been made are hopelessly out of date; only the Netherlands\textsuperscript{57} law and Italian\textsuperscript{58} laws have recent translations which have come to our attention. For neither is there any service in English to keep it up to date.

When we turn to the original sources, we find a confusing variety of arrangements. The famed "codification" of European law, whereby all laws are integrated in a single, compact, consecutively numbered collection, applies to business company laws in only three of the six countries—Belgium, Italy, and the Netherlands. In Belgium and the Netherlands the principal company laws are cited as a part of the Code of Commerce.\textsuperscript{59} In Italy, surprisingly, they are

\textsuperscript{58} For a short discussion of the evolution of Dutch commercial and company law, see Correa, \textit{La Pratique des Sociétés aux Pays-Bas}, 1 Rec. Prat. du M.C., Pays-Bas, Part 1.
\textsuperscript{58a} For a bibliography of sources which can be studied in English, see Szladits, \textit{International and Foreign Law Sources for the Business Lawyer}, 15 BUS. LAW. 575 (1960).
\textsuperscript{57} Internationaal Juridisch Instituut, Netherlands legal provisions of companies limited by shares (Netherlands 1957); \textit{Van der Meer, Dutch Corporation Law} (1959).
\textsuperscript{58} An English translation of Italian company law was published in 1957 by Mediolanum, under the title \textit{The American Investors' Digest of Italian Corporate Law}.
\textsuperscript{59} Belgium: \textit{Code de Commerce}, Liv. I, Tit. IX; \textit{Wetboek van Koophandel}, Boek I, Tit. IX.

Belgium: \textit{Wetboek van Koophandel}, art. 15–56h. There are, of course, general principles applicable to companies in many parts of the Civil Codes, especially in the parts on contracts of associations. There are also special corporation acts, like the Netherlands Act on cooperative associations, which are not integrated. The state-
cited as a part of the Civil Code,\textsuperscript{60} because of the achievement in 1942 of a long-sought-after unification of civil and commercial law. Even more surprisingly, they are found in the division of the civil law dedicated to labor law;\textsuperscript{61} this oddity reflects the "corporative state" concepts of fascism which were in vogue in the Italy of 1942, but it has no significant bearing on the content of the company law nor on the system of citing it.

In the other three countries the principal laws applying to companies have become quite separate from the commercial codes, as economic change has forced radical revisions of company laws while other portions of the commercial code retained more ancient dress. Of all the countries France has the most uncodified collection of company laws, reflecting the vicissitudes of national history almost as picturesquely as the architectural face of Paris.\textsuperscript{62} Some of the principles which underlie company law are still to be found in the Civil Code (Articles 1832–1873), although they yield, in commercial matters, to other general rules found in the Code of Commerce (Articles 18–46). For specific questions of French company law one must usually turn to particular laws which we will call the "Stock Company Law" and the "Limited Liability Company Law." But the French have no such handy names for them; they call them (respectively) the Law of July 24, 1867, and the Law of March 7, 1925.

The Stock Company Law has been greatly amended, so that not much more than its skeleton remains to witness the will of the 1867 legislator. The later legislators have sometimes despaired of hanging any more on the old skeleton, so we have further laws which certainly modify the effects of the law of 1867, but which are not framed as amendments to it, and must be separately cited. Notable examples are the laws of November 16, 1940, and March 4, 1943—both products of the "collaborationist" government at Vichy. Although neither the Stock Company Law nor the Limited Liability Company Law are formally parts of the Commercial Code, they are always contained as annotations in popular editions of the Code, along with the Vichy overlays and other supplementary legislation.

\textsuperscript{60} Codice Civile arts. 2247–2510.
\textsuperscript{61} Libro V "Del Lavoro."
The legal situation in Germany and Luxembourg is somewhat less confusing. Both have relatively modern and comprehensive company laws which are entirely separate from the Civil and Commercial Codes. Germany has a Stock Company Law, dating from 1937, and a separate Limited Liability Company Law dating from 1892. Luxembourg has a single Companies Law, separate from its codes, containing provisions on stock companies, limited liability companies, and other types of business association. The German company laws are contained in popular editions of the German Code of Commerce (Handelsgesetzbuch or H.G.B.), but the Luxembourg laws are available only in a separate booklet.63

The principal company laws to which we will refer repeatedly are shown on page 47 with the usual term of citation in the country of origin, and the abbreviated citations which we will use here.

B. THE CHOICE OF COMPANY FORM

1. THE KINDS TO CHOOSE FROM—AND THEIR NAMES

In five of the six Community countries—all but the Netherlands—the American lawyer who has decided to form a "corporation" will confront an initial puzzle. Each of these countries has not one, but two forms of business organization which may fairly be called corporations. Both are widely used, both are legal entities, both are taxed in essentially the same way, and both insulate their shareholders from liability for company debts.

These two forms bear witness to the European legislators’ desire to provide separate legal structures for the entities which Americans call "publicly held corporations," and those which we call "close corporations." One type of European company is empowered to offer its shares to the public, and list them on stock exchanges and is obliged to endure the glare of publicity on its financial affairs. The other type of European company is confined to offering its shares to a select few, has shares unsuitable for trading, and enjoys relative privacy. In these respects the European dichotomy appears much like the American.

But the American dichotomy is a differentiation of fact—a difference in how the shares are actually held and traded. Legally both kinds of companies (close corporations and publicly held corporations) belong to the same category ("business corporation," or

63 Recueil des lois concernant les Sociétés Commerciales (1956).
Country | Law | Cited in country of origin as: | Cited here
--- | --- | --- | ---
France | Stock Company Law | Loi du 24 juillet 1867, sur les sociétés | Law of 1867
| Limited Liability Company Law | Loi du 7 mars 1925, tendant à instituer des sociétés à responsabilité limitée | Law of 1925
Germany | Stock Company Law | Gesetz über Aktiengesellschaften ("Aktiengesetz") | AktG
| Limited Liability Company Law | Gesetz betreffend die Gesellschaften mit beschränkter Haftung (GmbH Gesetz) | GmbHHG
Italy | Civil Code, art. 2247–2574 | Codice Civile, art. 2247–2574 | C. Civ.
Luxembourg | Company Law | Loi du 10 août 1915 concernant les sociétés commerciales; Gesetz vom 10 August 1915, betreffend die Handelsgesellschaften 64 | Company Law
Netherlands | Code of Commerce art. 15–56h | Wetboek van Koophandel, art. 15–56h | W.K.

"corporations for profit"), they add the same distinguishing words or letters to their corporate name (Co., Corp., Inc. and the like), and they are formed under provisions of the same statute (for example, the Delaware General Corporation Law, or the Illinois Business Corporation Act). To pass from the "close" form to the "publicly held" form requires, at most, minor charter amendments, and the filing of securities registration statements.65

64 The provisions governing limited liability companies, although not adopted until 1933, are framed as an amendment of the law of 1915. Hence, we cite the "Law of 1915" for provisions which were not in effect until many years after that date.

65 The distinctions between the American close corporation and the European limited liability company have been brought out in a series of articles advocating that American states should adopt separate close corporation laws; see the following (in historical order): Weiner, *Legislative Recognition of the Close Corporation*, 27 Mich. L. Rev. 273 (1928–29); Rutledge, *Significant Trends in Modern Incorporation Statutes*, 22 Wash.
In Europe, on the other hand, these two kinds of company signify different legal categories, add different words or initials to their corporate names and are formed under different statutes. To pass from one legal form to the other requires the adoption of a completely new charter, through a procedure called "transformation."

American and English writers have used many different translations for these kinds of companies, frequently varying according to which European country is involved. For simplicity we will use the


I have chosen the term "stock company" for the Aktiengesellschaft or société anonyme, and the term "limited liability company" for the Gesellschaft mit beschränkter Haftung, or société à responsabilité limitée. The affirmative reasons for these choices are the following: (1) Neither term has a strong positive connotation in American law, such as to imply a greater parallelism than the laws justify. (2) Both terms are literal translations of the European terms in use in some or most of the countries surveyed. "Stock company" translates the German and Italian terms; "limited liability company" translates the French, German, Italian, Luxembourg, and Dutch terms, and barely misses the Belgian. (3) The two terms, both using the word "company," emphasize that they designate species of a single genus.

More compelling, however, than these affirmative reasons, are my objections to alternative terminologies which have been occasionally used or suggested: (1) "Anonymous company" or "nameless company" as a translation for "société anonyme" is the nadir of namesmanship. It connotes nothing. (2) "Corporation" as a translation for "Aktiengesellschaft" or "société anonyme" leads into a trap. If the SA-AG is also called corporation, we have got nowhere. If the SARL-GmbH is called some kind of "company," while the SA-AG remains a "corporation," the difference in terminology implies a greater difference in kind than really exists. The use of the term "corporation" leads into endless other difficulties. On the American side, the term properly includes such entities as municipal corporations, which are never signified by the corresponding European terms of société and Gesellschaft. On the European side, the "corporation" has cognates (corporation, corporazione, Körperschaft, corporatie) with quite different denotations. (3) "Close corporation" as a translation of GmbH or SARL is bad because the question whether a corporation is "close" or not is a matter of fact; whether it is a GmbH or an AG is a matter of law. An AG or SA can be closely held in fact, so that it corresponds functionally to an American "close corporation." (4) "Public company" and "private company" are perfectly usable terms with which to describe the European SA-AG and SARL-GmbH, respectively. They have disadvantages in suggesting an exaggerated parallelism between British and continental institutions. Further, the word "public" strongly suggests "governmental" to the American reader.

The following incomplete bibliography on others' usages may be of some interest:


same two translations, regardless of country. Our terminology is compared with the national originals as follows:

<table>
<thead>
<tr>
<th>Country</th>
<th>&quot;Stock Company&quot;</th>
<th>&quot;Limited Liability Company&quot;</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium:</td>
<td>société anonyme (SA)</td>
<td>société de personnes à responsabilité limitée (SPRL)</td>
</tr>
<tr>
<td></td>
<td>naamloze vennootschap (NV)</td>
<td>personenvennootschap met beperkte aansprakelijkheid</td>
</tr>
<tr>
<td>France:</td>
<td>société anonyme (SA)</td>
<td>société à responsabilité limitée (SARL)</td>
</tr>
<tr>
<td>Germany:</td>
<td>Aktiengesellschaft (AG)</td>
<td>Gesellschaft mit beschränkter Haftung (GmbH)</td>
</tr>
<tr>
<td>Italy:</td>
<td>società per azioni (SpA)</td>
<td>società a responsabilità limitata (SARL)</td>
</tr>
<tr>
<td>Luxembourg:</td>
<td>société anonyme (SA)</td>
<td>société à responsabilité limitée (SARL)</td>
</tr>
<tr>
<td></td>
<td>anonyme Gesellschaft (AG)</td>
<td>Gesellschaft mit beschränkter Haftung (GmbH)</td>
</tr>
</tbody>
</table>

The Netherlands is like the United States, and unlike the rest of Europe, in having only one statute under which both closely held and publicly held companies are formed. Companies of both types are legally called "naamloze vennootschap," just as both are legally called "corporation" in the United States. The initials "N.V." appear before or after the company name. If the company happens to be closely held, it may be described by bankers as "besloten," which means "closed." But the appellation of "besloten naamloze vennootschap" (like "close corporation") denotes a factual distinction, rather than a legal one. There is no widely used Dutch term for a "publicly held corporation."

Of course there are many other kinds of business associations, beside the stock company and limited liability company. In every country there are partnerships and limited partnerships, just as in the

"Corporation" (for SA-AG): FRIEDMANN et al., op. cit. supra; but cf. FRIEDMANN et al., THE PUBLIC CORPORATION (1954).
"Public companies and private companies" (for SA-AG and SARL-GmbH, respectively): Treillard, op. cit. supra note 66, at 546.
United States. There is also in most of the European countries a "limited partnership with shares," and there are a number of special purpose companies such as mutual insurance companies, cooperative associations, and credit unions.

None of these business associations seem likely to be of much interest to American traders and investors. Cooperatives and credit unions are inherently local. The limited partnership with shares is a survival of the slow evolution from partnership to stock company, comparable in its role to the American "joint stock company." Today it seems to offer no advantages which are not exceeded by those of the more usual stock company or limited liability company. The general partnership seems to be excludable as an avenue of American investment, since the participants become fully exposed to all the financial risks of a European businessman.

Partnerships:


Germany: Offene Handelsgesellschaft, Handelsgesetzbuch (hereinafter cited as HGB) §§ 105-160.


Italy: Società in nome collettivo, CODECIVILE §§ 2291-2312.


Limited Partnerships:


Germany: Kommanditgesellschaft, HGB §§ 161-177.


Italy: Società in accomandita semplice, CODECIVILE §§ 2462-2471.


The organizations referred to resemble limited partnerships in that some members are liable for firm debts, while others are not, but they differ from limited partnerships in their power to issue transferable shares. They have had a historical role as precursors of the modern stock company and limited liability company, somewhat like the role of the "joint stock company" in American law; but it would be quite misleading to call them "joint stock companies."

The following table indicates their various national names, and the laws applicable:


Germany: Kommanditgesellschaft auf Aktien, Aktiengesetz (hereinafter cited as AktG) §§ 219-232.

Italy: Società in accomandita per azioni, CODECIVILE §§ 2462-2471.


Netherlands: Commanditaire vennootschap op aandelen.
The limited partnership may deserve some consideration from a few American investors. Conceivably an American company could be a limited partner, while an individual (American or European) might be the general partner in Europe. European limited partnerships are very much like American limited partnerships under the Uniform Partnership Act, for the simple reason that the Anglo-American limited partnership is a business form which was directly and consciously copied from a European model. However, the number of American enterprises which would wish to participate in a European limited partnership would be very small, and we will not, in this paper, give further attention to this form.

The "holding company" has also received a good deal of attention in recent years from European writers and American observers. It is not, however, a distinctive form of organization; it is rather, as in the United States, the adaptation of one of the other forms of company (usually stock company or limited liability company) to a particular purpose.

2. THE LIMITED LIABILITY COMPANY—ITS PROS AND CONS

Most American corporations seem to have cast their European subsidiaries, except in Germany, in the mold of stock companies. On the other hand, European businessmen choose the limited liability much more often than the stock company; the ratio of preference in France was recently about 3 1/2 to 1 and was apparently even higher in Germany. Although many of the reasons why Eu-

---


71 The only European country of the Six which has a special holding-company statute is Luxembourg:
Loi du 31 juillet 1929 sur le régime fiscal des sociétés de participations financières (holding companies), reprinted in Recueil des lois concernant les sociétés commerciales (1956); Gesetz vom 31 Juli 1929 über die Besteuerung der Holdinggesellschaften, reprinted in "Gesetze betreffend die Handels, Holding-, und andere Gesellschaften" (1956).

However, the holding company is widely used in the Netherlands and other countries of the Common Market, without benefit of special legislative provisions.

72 A casual survey of well-known American subsidiaries in Europe has revealed no limited liability companies except in Germany. General Motors and Standard of New Jersey both have German sub-subsidiaries which are limited liability companies: Frigidaire GmbH, which is a subsidiary of Adam Opel AG (sub of General Motors); and Vereinigte Asphalt-und Teerproduktion Fabriken GmbH, which is a subsidiary of Esso AG (sub of Jersey Standard). Moody's Industrial Manual (1959) 1648, 2734. But Mr. Dieter Schneider, a lawyer of Cologne, states that "foreign subsidiaries in Germany are generally established in the form of a GmbH." The American Close Corporation and its German Equivalent, 14 BUS. LAW. 228, 249 (1958).

73 1 Rec. Prat. du M.C., sub. tit. Indications pratiques for France states that in 1957, 3270 SARL were formed, compared with 952 SA. The ratio of total companies in existence favors the SARL even more strongly.
Europeans might prefer the limited liability company do not apply to Americans, we believe that this form deserves more consideration than it has commonly received. We suspect that its unpopularity among Americans results partly from the fact that it looks strange and unfamiliar. We will, therefore, try to outline some of its distinctive features in various countries, starting with its disadvantages, and proceeding to some bases for preferring it.

a. Non-Negotiability of Shares

One feature of limited liability companies which will probably deter some investors is the non-negotiability of their shares. Stock companies in all the countries but Italy normally issue bearer certificates, which are transferred from one investor to another without any entry on the corporate books; the bona fide purchaser prevails over all prior claimants. In Italy stock companies no longer issue bearer shares, but registered shares are considered "negotiable" just as in the United States. Limited liability companies shares are never considered negotiable; they must always be transferred on the books of the company; in Germany the transfers must even be notarized; in Italy no certificates of ownership are issued. The buyer of a limited liability company share (with or without a certificate) takes it subject to any adverse claims of title, any claim of the company for unpaid share subscriptions, and any restriction on transfer, to which the transferor was subject.

In some, but not all, countries, there are further impediments to

---

In Western Germany, figures of companies in existence in 1955 showed 34,254 GmbH against 3,060 AG. Rec. Prat. du M.C., Indications pratiques for Germany.

74 Belgium: C. Com. I-IX, art. 45.
France: C. Com. art. 35.
Germany: AktG § 10.
Luxembourg: Company Law art. 37.
Netherlands: W.K. art. 38c.

75 Company Law (C. Civ. 2355) permits bearer shares as in other countries, but royal decrees have suspended the permission since 1941 (decrees of Oct. 25, 1941, and Mar. 29, 1942). Hence, all share transfers must be registered and are governed by C. Civ. arts. 2021-2027. But there is no provision, as in the limited liability company law, that transfers are ineffective even between the parties until registered.

76 Belgium: C. Com. I-IX, art. 125 (share transfer not effective until registered).
France: Law of 1925, arts. 21 (shares not negotiable), 23 (transfer incomplete until the company is formally notified).
Germany: Gesetz betreffend die Gesellschaften mit beschränkter Haftung (hereinafter cited as GmbHG) § 15. (requiring that all transfers be made with judicial or notarial formality).
Italy: Codice Civile art. 2479 (transfer ineffective until registered).
Luxembourg: Company Law art. 190 (transfer incomplete until the company is formally notified).
free trading in shares. In Belgium, France, and Luxembourg shares in a limited liability company cannot be sold to non-members without the consent of a specified majority of the other shareholders. This provision puts a minority shareholder at the mercy of the controlling group. It has been found so burdensome that Frenchmen often form a stock company in preference to a limited liability, even though they intend the company to be closely held.

This rule requiring consent to transfer does not apply in Germany and Italy, unless it is voluntarily inserted in the corporate charter.

b. Exclusion from Financial Markets

A second disadvantage of the limited liability company is the fact that it cannot raise money by public issue of stocks and bonds, nor can its securities be traded on the securities markets. Some of the countries have a specific prohibition against public issue or trading. In others the same effect is achieved by prohibitions against issuing the kinds of securities which outside investors would want to buy. One of these prohibitions is the one on issuing negotiable shares, explained in a preceding paragraph. A further prohibition, effective in Belgium, France, Italy, and Luxembourg, prohibits the issue of bonds—that is, debt securities in forms designed for sale to small investors.

These prohibitions do not prevent limited liability companies from financing themselves from private sources. The rules about stock would be no impediment to shareholding by a select group of individuals nor, except in Belgium, by a parent or a consortium of investing companies; only the general public are excluded. Likewise loans can be "privately placed" with banks and insurance companies. Since public issues of bonds are relatively less important in Europe than in the United States, the inhibition on public bond issues will probably not make much practical difference to a company until it becomes very large and well-known.

78 Germany: GmbHG § 15(5). Italy: C. Civ. art. 2479.
79 Luxembourg: Company Law. art. 188. France: Law of 1925, art. 37.
c. Other Disadvantages

A few other special features of the limited liability company which may deter its use at particular times and places must be mentioned. Belgium has a peculiar rule requiring that all shareholders be natural persons and not corporations. Our Belgian collaborator regards this as a rule of substance, not form. Hence the limited liability company must be written off as a form of corporate subsidiary in Belgium; but it might make a good affiliate for an American close corporation, whose principal shareholders could also hold shares in the Belgian limited liability company.

France has a rule of income taxation whereby the salaries paid to majority shareholders of a limited liability company are regarded as profit distributions, rather than as wages, and incur a 22% basic tax (before the progressive surtax) instead of the 5% payroll tax which falls on salaries of stock company officers. This has driven many French businessmen to desert the limited liability company in favor of a stock company; but it will not be any problem to American-owned limited liability companies, since it is unlikely that their salaried officers will be majority shareholders. We presume that shares will be held by corporations rather than individuals.

Italy has a set of unfavorable tax rulings which have been applied to the limited liability company. On the one hand, its profits are subjected to the corporation income tax, which partnerships and individual enterprises escape; on the other hand, its share transfers are subjected to a business transfer tax which corporation shares escape. Thus it has double disadvantages. Until one of these inconsistent rulings is abandoned, the limited liability company must be avoided in Italy; but our collaborators view this problem as temporary. When it is solved, the Italian limited liability company may be a relatively attractive form of enterprise.

Most of our collaborators report that the limited liability company is viewed with suspicion by creditors, because it has been so often used for under-capitalized enterprises which eventually failed; the stock company on the other hand enjoys a presumption of financial responsibility. We suppose, however, that the presumption against the limited liability company is readily rebutted by evidence of adequate capitalization, or by the parent company's willingness to guarantee particular undertakings.

---

81 Belgium: C. Com. I–IX, art. 119.
d. Restrictability of Share Transfers

We referred above to restrictions on transfer as possible disadvantages in the limited liability company. Restrictions are a disadvantage to a capitalist who wants to induce maximum financial participation in his company by outside investors.

But we have found that many American corporations, contemplating investments in foreign countries, are much more concerned with keeping investors out than with getting them in. Such corporations issue a very minimum of shares to others than the parent corporation itself, and require each recipient to agree in writing to make no disposition without consent.

Where the desire is to minimize public participation in the company’s equity, the limited liability company offers definite attractions. In Belgium, France, and Luxembourg the shares are automatically non-transferable unless a specified majority of the other shareholders consents. In Italy and Germany the law does not impose this restriction, but permits its insertion in the company charter.

It is true that some degree of non-negotiability is also attainable in stock company shares. Professor Houin believes that the numerical majority of French stock companies would be found to have rules restricting stock transfer. But restrictions on transfer are not expressly authorized by the stock company laws of most countries, and the extent to which transfers may be validly restricted is not clearly defined either by case law or by legal theory.

---

83 Germany: GmbHG § 15 (expressly stating that transfers may be restricted by charter provisions). Italy: C. Civ. art. 2479 (stating that shares are transferable in the absence of contrary provisions in the articles of incorporation) (salvo contraria dispozione dell’atto constitutivo).
84 Germany expressly authorizes charter restrictions on transfer: AktG § 61 (3). But many desired forms of restriction are beyond the statutory authorization: See SCHLEGEL-BERGER-QUASSOWSKI, KOMMENTAR ZUM AKTIENGESETZ § 71, Anmerkung 9 (1939).
85 An interesting exchange of views on the subject in Belgium is contained in a pair of comments by Coppens, 64 JOURNAL DES TRIBUNAUX 215 (Belgium 1949), and de Rouvreux, 55 REVUE PRATIQUE DES SOCIÉTÉS CIVILES ET COMMERCIALES 54 (Belgium 1956); cf. VAN RYN, PRINCIPES DE DROIT COMMERCIAL, Part I, at 364 (1954); for Germany see Schneider, op. cit. supra note 66, at 233.
e. **Number of Shareholders**

A second feature of the limited liability company which may attract some Americans is the smaller number of shareholders required. In Belgium, France, and Luxembourg a stock company requires seven shareholders, while a limited liability company requires only two. According to the prevailing view of lawyers in these countries, the shareholders must be bona fide in that they must pay their own money for their shares. But they need not hold more than one share a piece; and they may be bound by contract to assign the share to someone else on demand of the parent company.

European lawyers generally do not consider shareholder requirements as a weighty consideration. Even if they are violated, the principal consequence (in Belgium, France, and Luxembourg) is liability to an annulment proceeding, which in France can be arrested by restoring the number of shareholders to seven (provided they have never dropped below two). Since a shareholder’s derivative suit cannot be brought by less than five percent of the shareholders, European lawyers have no such fear of small shareholders as American lawyers generally do.

Whatever the merits of this European view may be, we believe that most American parent companies in fact will be extremely cautious in the selection of the other six shareholders, and in maintaining amicable relations with them. The time and trouble involved in finding six such shareholders and keeping them happy can be cut down by using the limited liability company form, which requires only one shareholder in addition to the parent company.

The difference in required number of shareholders has less significance in the other countries. In Italy two shareholders are enough for either type of company. Even if there is only one, the company does not cease to exist; it merely ceases to insulate the sole shareholder from personal liability for debts of the company. In Germany there is a difference in the number of incorporators required

---

86 Belgium: C. Com. I–IX, art. 29.  
France: C. Com. art. 23.  
87 Belgium: C. Com. I–IX, art. 119.  
France: Law of 1925, art. 5.  
Luxembourg: Company Law art. 183.  
88 Cf. Lepaulle and Jeantet in FRIEDMANN, LEGAL ASPECTS OF FOREIGN INVESTMENT (1959) at 214, 220–221.  
89 Ibid.  
90 Italy: C. Civ. art. 2247.  
91 Id. art. 2362.
(five against two), but there is no objection to 100% ownership by a single shareholder after the company is once formed. Hence the selection of the extra incorporators does not demand much attention in either Germany or Italy. The Netherlands has no limited liability companies, but two incorporators are enough to form a stock company, and the number of shareholders after incorporation does not need to be more than one.

f. Number of Officers and Directors

A third attractive feature of the limited liability company is the simplicity of management structure permitted by law. A small limited liability company can operate with no board of directors, no president, no auditors and only a single manager. It is not even necessary to hold a shareholders’ meeting to elect the manager; he may be named in the articles, and hold office indefinitely without the necessity for annual elections.

This simple arrangement is not recommended as a permanent structure in any company; but it may be extremely convenient in the early years of a foreign venture. The parent company may not know to whom it can wisely entrust the decision-making power in a European country; it will hope to avoid naming board members whom it may later wish to remove and replace.

In contrast, the stock company is required by law to provide itself with a panoply of officialdom which is sometimes quite premature. The requirements are most elaborate in Germany, where every

---

92 AktG § 2: Five members; GmbHG § 2: Specifying no number, but implying plurality.
93 BAUMBACH-HUECK, AKTIENGESETZ § 30 (9 ed. 1956).
94 Belgium: C. Com. I–IX, art. 129. But a board of auditors must be named, if there are more than five shareholders. Id., art. 134. The single manager is called a gérant, or beheerder.
France: Law of 1925, art. 24. But if there are more than 20 shareholders, a board of supervision (counsel de surveillance) must be named, id. art. 32. The single manager is called gérant.
Germany: GmbHG § 6. But there must be a supervisory board (Aufsichtsrat) if there are over 500 employees, by the terms of the Betriebsverfassungsgesetz of Nov. 10, 1952, § 77. The single manager is called a Geschaftsfiihrer.
Italy: C. Civ. art. 2487. But an auditing committee (collegio sindacale) is required if the capital is over 1,000,000 lire (about $1500). Id., art. 2488. The single manager is called an amministratore unico.
Luxembourg: Company Law art. 191. There is no limit on the size of the company which may be governed by a single manager, called gérant or Geschäftsfiihrer.
95 Belgium: C. Com. I–IX, art. 129.
Germany: GmbHG § 6.
Italy: C. Civ. arts. 2487 and 2383.
Luxembourg: Company Law art. 191.
stock company must have a supervisory board (*Aufsichtsrat*) of three or more members, none of whom are either executives or employees of the company, and who must hire one or more executives (*Direktoren*). In other words, the investor in a stock company must find three policy-makers whom he trusts enough to put them in charge of his business, but who are not employed in it, plus one full-time executive. In a limited liability company he needs to find only the executive.

A similar number of persons must be found in Italy—at least three auditors (*sindaci*) who are neither employees of the company nor relatives of the manager, and at least one manager (*amministratore*). But the choice is a little less momentous, since the three auditors do not have the extensive powers of the German supervisory board.

In France and Belgium, four persons must also be found to fill the necessary positions—three managers (*administrateurs*) and at least one auditor (*commissaire*). The directors may be employees of the company, but the auditors must be strictly independent—not employed by the directors or by the company, and not related by blood or marriage to the directors. The requirements are the same in Luxembourg, except that there are no express prohibitions of other relations between the auditor and the company or its directors.

The privilege of operating a limited liability company with a single manager is available only to “smaller” enterprises, but the criteria of smallness vary greatly. In Italy, the line is drawn at the meager capital of 1 million lire (about $1,500); above that, auditors are required. In Germany, the line is drawn at 500 employees; with more, a 3-man supervisory board is required. In Belgium and France, the line is drawn in terms of number of shareholders; such a line need never be crossed by a typical corporate subsidiary. The penalty for crossing is a three-man board of auditors. Only Lux-

---

86 AktG §§ 70, 86, 90.
87 C. Civ. arts. 2380, 2397, 2399.
88 France: Law of Nov. 16, 1940, art. 1 (*administrateur*); Law of 1867, art. 32 (*commissaires*).
89 Belgium: C. Com. I–IX, arts. 55 and 64.
90 France: Law of 1867, art. 33.
91 Belgium: C. Com. I–IX, art. 64 quater (as amended by law of Dec. 1, 1953).
92 Luxembourg: Company Law art. 61.
93 Italy: CODICE CIVILE art. 2488.
94 Betrieberversammlungsgesetz § 77 (Hereinafter cited as BetrVerfG).
96 France: Law of 1925, art. 32.
LUXEMBOURG SETS NO STATUTORY SIZE LIMIT TO THE COMPANIES WHICH MAY USE THE SINGLE-MANAGER SYSTEM: PERHAPS SIZE LIMITS IN LUXEMBOURG ARE IMPOSED BY GEOGRAPHY.

The weight which should be given to these personnel requirements varies somewhat among the countries. A few officers, like the executives (Direktoren) in a German stock company, cannot be removed from their position without proof of unfitness for the office. Most officers—including the members of the highest governing boards in France and Germany (conseil d'administration, conseil de surveillance, Aufsichtsrat) are removable at the pleasure of the shareholders.104 As to officers of the latter type, the investor can if necessary authorize his European counsel to fill the positions with docile individuals who will vote as instructed, and resign when requested; that is, with "dummy directors." Certainly the difficulty of filling positions should not stand in the way of selecting a form of organization which is strongly indicated by the financial requirements of the enterprise. But, other things being equal, useless cogs in the administrative machinery are to be avoided for the same reason as are useless parts in the power plant.

g. Labor Representation

In Germany a unique factor favoring the limited liability company is encountered. In every stock company, regardless of size, one-third of the supervisory board members (who choose the executives) must be labor representatives. This requirement does not affect limited liability companies until they have 500 or more employees.105

h. Privacy

A few American investors may also be attracted to the limited liability company by the greater financial privacy permitted in some countries. In Germany and Luxembourg stock companies must publish their annual financial statements,106 while limited liability companies do not have to. But the resulting disclosure is no greater, and usually less, than unlisted American corporations' statements in Moody's or Standard and Poor's.

104 For a fuller discussion of "governing boards" see the next part of this chapter, under the title "Management of a European Subsidiary."

105 BetrVerG §§ 77.

106 Germany: AktG § 143.

Luxembourg: Company Law art. 75. In France, the duty to publish financial statements falls only on those stock companies which are listed on a stock exchange. Ord. 59-247, Feb. 4, 1957; J.O. Feb. 8, 1959, p. 1754; L'ACTUALITÉ JURIDIQUE 1959, III. 62.
i. Other Advantages

There are other advantages in the limited liability company form which contribute to its popularity among small businessmen in Europe. One of these is a smaller minimum capital; in Germany a stock company must have minimum capital of about $25,000, while $5,000 will do for a limited liability company. Another is the simplicity of the papers to be filled out; they are such that a European businessman may feel safe in preparing them without a lawyer. Some laws permit publishing an extract of limited liability company articles, while stock company articles must be published in full at greater expense. These advantages will not be of much interest to American investors in Europe; they are pin-prick in relation to the major expenses and difficulties inherent in a trans-Atlantic plunge.

3. TRANSFORMATION

The choice between stock company and limited liability company, once made, is not irreversible. In each country which offers the choice, there is also a procedure for changing from one to another, called "transformation." Like incorporation, it involves drawing up new articles, and depositing and publishing various copies or extracts; the expenses are probably about the same as for incorporation.

However, transformation is not necessarily a "tax-free reorganization," in the American sense. In Belgium and Germany, at least, it is viewed under tax laws as a sale of assets unless it comes within certain strict limitations. If it is not within these limits, it incurs transfer taxes based on the value of the assets transferred, and income tax on previously unrealized or unreported gains. In Germany, the limits are fairly wide; it is sufficient that both companies (the submerging, and the emerging) are German, that 100% of the assets pass in exchange for stock in the new company and that the

107 AktG § 7 (100,000 DM minimum for a stock company), GmbHG § 5 (20,000 DM minimum for a limited liability company).

The minima are even lower in other countries; Italy requires 1,000,000 lire (about $1500) for a stock company and 50,000 lire (about $75.00) for a limited liability company. C. Civ. art. 2327, 2474.

108 Belgium: The procedure is nonstatutory.
France: Law of 1925, art. 21 (Transformation).
Germany: AktG §§ 264-277 (Umwandlung).
Italy: CODICE CIVILE art. 2498 (Trasformazione).
Luxembourg: Procedure is nonstatutory.
book entries be such as to negative any concealment of tax liability. In Belgium there is no statutory exemption, but only a practice of the treasury not to claim taxes in those cases in which both the members and the assets of the company remain the same after the transformation as before. In France, on the other hand, transformation seems to be tax-free by general rule.

We understand that the burdens and risks of transformation are enough to deter the ordinary incorporator from forming a limited liability company with the intention of transforming it to a stock company a few years later, or vice versa. The form is chosen for "keeps," although later events sometimes lead the choosers to reverse their original choice. The situation is not like that of England or the United States, where every company is born as a "private company" or "close corporation," and becomes a "public company" or corporation of "public issue" by virtue of later acts. In Europe, it is usual for the lawyer to attempt to foresee the ultimate character of the enterprise, and to incorporate in the form which is appropriate to that ultimate character.

C. THE CHOICE OF A STATE OF INCORPORATION

I. THE DETERMINING FACTORS

One of the features of European incorporation which differentiates it most sharply from incorporation in the United States is the absence of freedom of choice of the state of incorporation. The European lawyer who is forming an operating company does not incorporate in the country whose tax or corporation laws are most favorable, without regard to where the company's headquarters are going to be. His choice is already made by the client who has decided, for other reasons, where he wants to locate the "central office" of the business.¹⁰⁹

The reasons for this absence of freedom are connected with two rules of law. One of these is a rule found in the corporation statute for each country, which provides that the articles must designate a central office (siège, Sitz, sede, zetel) which must be, at least inferentially, in that country.¹¹⁰ In this respect they differ from the

¹⁰⁹ I adopt for use in comparative law the term employed by RABEL, 2 CONFLICT OF LAWS 31 ff. (1947). Since this concept is not used in Anglo-American law, there is no precise legal parallel, although it is much like the "home office" of an insurance company.

¹¹⁰ All the laws require that the articles of incorporation be filed at the commercial court or commercial registry, or both, of the district in which the company has its
Delaware act, which requires designation only of "the principal office . . . within this state," 111 or the Illinois act, which calls for "the address . . . of its initial registered office in this State." 112 A classic view among European theorists is that if the actual central office is in a country other than that of the office designated in the articles, the company is in violation of its charter, and is exposed to various undesirable (if unspecified) consequences.113 A few contemporary writers have questioned whether there are really any serious consequences to be feared,114 and a Dutch authority declares that the Dutch Minister of Justice often ignores known violations of the rule.115 The Italian law specifically permits a company to adopt, by amendment, of its charter, a foreign central office.116 But in companies other than the Netherlands and Italy, an American-owned enterprise would be unwise to make a deliberate test of the rule.

The second rule which inhibits freedom of choice of place of incorporation is a rule of conflicts of laws. According to prevailing European opinion, a corporation's internal affairs and its legal existence are governed by the law of the place where the central office is located.117 This seems to mean the actual central office, not a "central office," in terms which leave no doubt that a court or registry in the country of the legislator is intended. See, for instance:

France: Law of 1867 art. 55.
Germany: AktG § 28.

The Netherlands law specifically states that the central office (plaats van vestiging) must be within the Netherlands. W. K. art. 36c. There are exceptions in the Netherlands and elsewhere, enacted in contemplation of enemy occupation, which permit temporary removal of the central office for emergency reasons which will not enter into the planning of American investors.

112 General Corporation Law of the state of Delaware § 102(g) (2). The wording admits the possibility of other "principal offices" in any number of other states.


114 Ripert, Tracté Élémentaire de Droit Commercial 268 (France 1954).
Von Godin-Wilhelmi, Aktiengesetz § 5, Anmerkung 6 (Germany).

115 Kollewijn, American-Dutch Private International Law, No. 3 Bilateral Studies in Private International Law 16 (1955). Kollewijn is somewhat sceptical of this view, but recognizes it as "prevailing."

116 See Beitzke, Juristische Personen im International Privatrecht und Fremdenrecht 104 (Germany 1938).

117 See Kollewijn, op. cit. supra note 54, at 16.

118 C. Civ. art. 2437.

119 Rabel, 2 Conflict of Laws 33-37 (1947).

120 Batiffol, Tracté Élémentaire de Droit International Privé 232, 453 (France 1955).


This view was crystallized in a uniform law contained in a treaty signed by the Benelux countries, but which never came into effect because it was never ratified by
fictitious one stated in the articles. This contrasts with the prevailing American rule that the corporation’s existence and internal affairs are governed by the state of incorporation, wherever it may establish its central office. Following this theory it is said that a company which is organized under the laws of one country, and then sets up a central office in another, is invalid at the situs of its central office, because it has not organized in accordance with the laws prevailing there.

Professor Ernst Rabel, discussing this question in terms of a Delaware corporation doing business in Europe, declared:

A corporation constituted in Delaware with headquarters in Amsterdam will be considered subject to Dutch law on the whole European continent, and therefore on principle as non-existent.

While the essence of the rules has often been misunderstood especially in the English literature and by German writers too, the policy behind the rules has not always been appreciated. The most important viewpoint from which to consider the rule is of a state that does not want an organization to establish its principal office in its territory and yet derive its existence and legal character from a foreign state. Thus, in the oldest decisions of the German Supreme Court on this matter, a company incorporated in the state of Washington, United States, for the purpose of exploiting Mexican mines, but which was controlled by a board of directors in Hamburg, Germany, the Netherlands, as the Hague Treaty of May 11, 1951. It stated in Article 3, “The existence of a legal person and its organs or representation shall be determined by the country of its seat. For the purposes of this Article, an artificial person shall be considered to have its seat at the place where its central control is located.”

These provisions, which have no legal force, are regretted by Kollewijn. According to our informants, these provisions are a major obstacle to ratification, and may be dropped.

The rule that the company is governed by the law of its central office is apparently codified by the laws of Belgium and Luxembourg, both of which provide in identical terms that “every company whose principal establishment is in Belgium (in the Grand Duchy) is subject to the Belgian (Luxembourg) law, even if the incorporation took place in a foreign country.” Belgium: C. Com. I–IX art. 197;

Luxembourg: Company Law art. 159. This seems to be understood as referring to the central office, rather than to the site of exploitation.

Italy: The code declares that all companies are subject to Italian company law if they have their central office or principal activity in Italy (C. Civ. 2505), although inconsistently declaring that Italian law applies to companies formed in Italy, but active principally abroad (C. Civ. 2509). See also Loussouarn, Droit International du Commerce, Revue Trimestrielle de Droit Commercial 246, 250 (1959), commenting on art. 58 of the Treaty of Rome.


was denied recognition as an American legal entity; having failed to fulfill the German requirements for incorporation, it was treated as a German non-corporate association. When a domestic company transfers its domicil to a foreign country, it loses its personality. 120

In the view of our Dutch collaborator, Professor Rabel's choice of Amsterdam as a hypothetical site was unfortunate. Mr. Deelen concurs in Kollewijn's view with respect to a corporation formed under foreign law but having its actual central office in Holland, that

It is out of the question that a Dutch judge would ever, on this sole ground (there being no fraud or public policy considerations) declare a corporation null and void, and no decision to that effect has ever been rendered. 121

Conversely, he believes that corporations could be formed in the Netherlands, and operate their affairs from headquarters in Germany or France without objection from the Dutch government or courts.

However, an investor cannot safely take advantage of this Dutch liberalism unless he is assured of equally tolerant views in the neighboring countries in which the other part of the play would have to be acted. Despite intimations of similar tolerance by occasional writers in other countries, 122 the weight of authority (and of our collaborators) cautions against experimenting with these rules of law. The safe course is to organize where the central office is to be, and to centralize management unambiguously at that office.

Although there is no freedom to choose a state of incorporation which is different from the state of the central office, there is no prohibition against choosing a central office location which is outside the country of the principal business operations. 123 For instance, a company could establish its main office in Luxembourg, although its principal business consisted of exploiting coal mines in the Netherlands or operating steel mills in France. The "central" office is

---

120 RABEL, op. cit. supra note 117, at 37-39.

The result seems to be precluded also by the Netherlands-U.S. Treaty of Friendship, Commerce and Navigation, which provides in Article XXIII, § 3, that "Companies constituted under the applicable laws and regulations within the territories of either party shall be deemed companies thereof, and shall have their juridical status recognized within the territories of the other party." T.I.A.S. 3942.
122 E.g., Beitzke, op. cit. supra note 114.
Ripert, op. cit. supra note 113, at 396.
Battifol, op. cit. supra note 117, at 232.
Wolf, op. cit. supra note 117, at 115.
Rabel, op. cit. supra note 117, at 40.
identified by reference to activities of management and supervision, rather than activities of manufacture and sale.\textsuperscript{124}

According to our information, little use is made, and little should be made, of this technical freedom. It is quite unlike operating a Hoboken refinery from a Manhattan executive office, because there are between any two European countries a flock of actual or potential barriers which have not existed since 1865 between American states. There are passport clearances impeding travel from one to the other, differences of currency, possible exchange restrictions, and customs (until 1972). All these barriers impede the intimate contact between management and operations which is just as essential to optimum efficiency in Europe as it is in the United States.

There is another reason for not separating management from operations which is peculiarly European. European managers with whom we have spoken emphasize the necessity of constant contacts with government, since price changes, wage changes, and major building programs must frequently be approved by an official of a national ministry. It is reliably reported that the notoriously uneconomic concentration of French industry in the Paris area is influenced by the need of managements to be simultaneously near their plants and near their ministers.

Consequently, it is unlikely that a company organized to mine or manufacture solely in France would locate its central office in Germany or vice versa. However, if a single company were formed to mine and manufacture in both France and Germany, it might locate its central office in either of the countries, and would not need to move because the activities in the foreign country grew larger than those in the country of the central office. Or it might choose a central office in Luxembourg, which is between the major countries.

2. THE "DELAWARES OF EUROPE"

If we may judge from our conversational contacts, the views expressed in the preceding paragraphs will surprise many American lawyers, who have been told that Lichtenstein or Switzerland or Luxembourg is the "Delaware of Europe."

Such metaphors convey more falsity than truth. In so far as they suggest that these countries furnish a convenient place for incor-

\textsuperscript{124} Loussouarn, in \textit{Les Conflits de Lois en Matière de Sociétés} 135 (1949) contends that a central office which did not coincide with any important operations would be presumptively fraudulent.
porating a company which will have its central office and principal operations in other countries, they are false both in law and in practice. None of these countries is commonly used, or could be advantageously used, for such purposes, for the reasons already given.

A second connotation of such a metaphor might be that the laws of these countries permit great freedom in financial operations, for instance, the payment of "nimble dividends" when capital is impaired, or the assignment of most of the share consideration to surplus which can be freely paid out as dividends. These suppositions would also be baseless, at least as to Switzerland and Luxembourg.

Or it might be supposed that these countries have lower incorporation fees than neighboring countries, as Delaware's franchise tax is lower than that of most industrial states. We do not have complete information on the incorporation fees in these countries, but we understand that incorporators are not drawn to them by cost advantages of this kind.

However, it is true that certain investors have sought out these countries as places in which to incorporate and manage their companies, in preference to neighboring countries; but the companies so formed have been, in almost all cases, holding companies, not operating companies. They have been truly localized in the country of incorporation, because their securities are kept there.

D. THE European Lawyer's Role in Incorporation

The procedures of incorporating in the countries of the European Common Market are basically like procedures in the United States. They start with some rather mechanical documents, filled with the proper number of names and addresses, indications of the corporate purposes, statements of kinds and amounts of capital stock, and a good many paragraphs about directors and officers, their powers and their pay. The papers must be filed, some sort of publication made, fees paid, organization meetings held, and certificates of completion of one or another formality carefully executed.

In Europe, as in the United States, these formalities are for the local practitioner. There is no point in the American investor's learning their details, because he cannot perform them anyway. Hence, we do not present checklists of incorporation steps.

What the American investor can do is to make an intelligent selection of a European practitioner, explain his general objectives, and review the documents which the practitioner proposes to file and
publish. The following observations explain some of the differences in European practice which an American investor will encounter in his dealings with European legal representatives.

I. THE ADVOCATE

The American who looks around the Common Market for a "corporation lawyer" encounters a puzzling situation. It is difficult to find any expression in any of the four languages involved which would accurately translate the term "lawyer," much less the term "corporation lawyer."

The American may, however, ask for a "member of the bar," and be led without hesitation to an "advocate" (avocat, Anwalt, advocato, advocaat). The advocate is primarily a courtroom lawyer and is often compared to the English barrister. But, unlike the barrister, he does not have to be approached through a solicitor, nor does he expect the facts to be gathered and the case appraised before it comes to him. Perhaps the advocate is best explained by saying that he is like one of the great general practitioners of America's nineteenth century, who could try a tort case, argue a constitutional law appeal, and advise a corporation on its tax liability, all without partners or junior associates.

Many European advocates, including some of the very best, are solo practitioners, except as they may have apprenticed assistants. In France group practice among advocates was forbidden until 1954. Since solo practitioners are not likely to be highly special-

126 See Burdick, The Bench and Bar of Many Lands (1939), for general observations on the legal professions in Germany, France, and Italy. For France, see Lepaulle, Law Practice in France, 50 Colum. L. Rev. 945 (1950); Brown, The Office of Notary in France, 2 International and Comparative Law Quarterly 60 (1953); Tunc, Modern Developments in Preparation for the Bar in France, 2 J. Legal Educ. 71 (1949-50); Simmons, French Lawyers' Special Fields, 30 Tulane L. Rev. 101 (1955). For Germany, see Weniger, The Profession of the Bar in Germany, 34 Ill. L. Rev. 85 (1939-40). For Italy, see Sereni, The Legal Profession in Italy, 63 Harv. L. Rev. 1000 (1950).

The plurality of possible interpretations is illustrated by the fact that Frenchman Tunc (above) treats avocats and avoués as the only classes of French lawyers, while Frenchman Lepaulle (above) described avocats, avoués, notaires, and agents d'affaires as varieties of "lawyers."

127 For instance, by Brown and by Tunc (see note 125 supra). With respect to France, there is some point in the barrister-advocate comparison because neither has power to "represent" (i.e., make binding agreements for) his client; that belongs to the solicitor in England and the avoué in France. But the comparison may prove misleading, since the French advocate does not have to be briefed by a solicitor (as the English barrister does), and cannot file written pleadings (as the English barrister can).

In other countries, the advocate may bind his client.

128 Hamelin, Abrégé des Règles de la Profession d'Avocat art. 207 (1954), citing decree of April 10, 1954, art. 49.
ized, in corporate matters, many advocates will not draft the incorporation papers in their own offices. Some, of course, will do so. Others may accept the responsibility, but delegate the work to an outside office to prepare the documents—especially if the American client seems to expect that the advocate should himself produce the papers. An equally normal procedure, in most of the Common Market countries, is for the advocate to discuss the principal problems, advise the client on some of the preliminary questions (what form of company, where to incorporate, what kind of management structure) and then send the client on to a notary to get the drafting done. In some of the German states (Länder) the offices of advocate and notary are combined; in these states it is most probable that an advocate will be found who is both a counselor on corporate matters and a draftsman of corporate documents.

2. THE “ATTORNEYS-OF-RECORD”

In France there is a special kind of lawyer called an “avoué”—a title whose etymological connotations recall the English “attorney.” We mention the avoué only because the identification of French “advocates” with English “barristers” leads so easily to the identification of French avoués with English “solicitors.” Since a prospective American investor in England would properly consult an English solicitor, the conclusion might be drawn that an American investor in France should consult a French avoué.

Nothing could be further from the mark. The job of the avoué is to appear of record for a litigant, to file written pleadings, to receive notices, and to make on behalf of the client any commitments and elections which are incident to the procedure of litigation. The pleadings which are filed by the avoué may be drawn either by himself or by the advocate, but oral advocacy is the job of the advocate. An American translation for this peculiar intermediary might be “attorney-of-record.”

These functions of this “attorney-of-record” are much like some of those performed by an English solicitor. But the French “attorney-of-record” performs none of the functions of business counseling, property management, and drafting of non-litigious documents, which probably occupy the larger part of an English solicitor’s

---

128 The distinguished comparatist Tunc compares them for certain purposes. *Op. cit.* supra note 125, at 71, n. 1. Tunc emphasized that the French avoué, like the English solicitor, has the power to “represent” his client.
time, and which qualify him to advise an American investor. Most of these functions are performed in France chiefly by notaries.\textsuperscript{129}

The "attorney-of-record" is a professional who is peculiar to France, and is not even found in all districts of that Country. There is some recognition in other countries of the attorney-of-record's distinct functions, but they are generally performed by a person who bears the title of "advocate."\textsuperscript{129a}

3. THE NOTARY

The European notary is also a lawyer.\textsuperscript{130} That is, he is a man who has a university law degree, or who has at least passed professional examinations for his position, and who makes his living strictly by professional work. But he generally does not appear in court, except when, as in some German states, he is also an advocate. Since notaries handle almost all aspects of the administration of decedents' estates, marriage settlements, and conveyances of real estate, they might remind an Englishman of a family solicitor; an American colleague might call them "office lawyers." But the European notary has a dignity which distinguishes him from either an English solicitor or an American lawyer. Like an American justice of the peace, he exercises a public trust, even though his income depends on private fees. He holds an "office" which he has either inherited from an ancestor or purchased at a high price, and he is a custodian of records of property ownership. When he takes acknowledgments of documents, he is not satisfied by knowing that the signature is genuine; he will read or explain the entire document to the client, and refuse to take the acknowledgment unless he is quite sure that the client understands every line. In fact, the notary is normally the draftsman of documents whose acknowledgments he takes.\textsuperscript{131}

Urban notaries frequently become specialists in corporate prac-

\textsuperscript{129} Cf., Brown, \textit{op. cit. supra} note 125, at 60.

\textsuperscript{129a} In Italy, a young lawyer is first admitted to practice only as an attorney-of-record (\textit{procurazione}), but later becomes an advocate (\textit{avvocato}), and thereafter performs both functions. See Sereni, \textit{supra} note 125.

In Luxembourg, most lawyers describe themselves as being both advocates and attorneys, using the hyphenated title, \textit{avocat-avoué}.

\textsuperscript{130} See Schlesinger, \textit{The Notary and the Formal Contract in Civil Law}, NEW YORK STATE, REPORT OF THE LAW REVISION COMMISSION 403 (1941) (observations on France, Germany, and Switzerland).

Brown, \textit{op. cit. supra} note 125, at 60.

\textsuperscript{131} Our Netherlands collaborator says that in his country the notary invariably drafts any instrument which is required to be notarized.
tice. It is no accident that some of the best French treatises on company law have been written by the editor of the "Notaries' Journal." 132

4. UNLICENSED LAWYERS

Various classes of people who are not members of any legal profession, and perhaps not of any licensed profession, also participate actively, competently, and lawfully in advising on incorporation problems. Frequently tax problems are important, and these will probably be referred by lawyers or notaries to tax specialists, who are not usually lawyers; they are sometimes, but not necessarily, accountants.

Accountants may also assume the main work of planning the corporate organization and drawing the papers; an Italian advocate has advised us that his accountant competitors are perfectly competent in corporate matters, while another doubts it.

There are also, at least in France, wholly unlicensed business agents (agents d'affaires or conseillers commerciaux) who will undertake to arrange an incorporation, acting partly as advisers and partly as intermediaries for notaries and tax specialists who may be needed.133

Some of these unlicensed advisers have organized themselves into an association of "company legal advisers" (conseils juridiques de sociétés). The existence of these unlicensed operatives in a semilegal field seems to be an indirect result of the fractionation of the French legal profession in terms of formal procedures—formal appearance and filing of written pleadings (by the avoué),134 oral argument (by the avocat), and drafting of nonlitigious documents (by the notaire). As an incident of this fractionation, counseling has become nobody's profession.

This interesting lacuna in French professional regulation explains the role of the many American lawyers in Paris who have no license for any kind of practice in France. So long as they only give advice, referring formal procedures to licensed attorneys-of-record,


133 See Lepaulle, op. cit. supra note 125, at 947; Simmons, op. cit. supra note 125.

134 In discussing French procedure (in English) one must distinguish between the written contentions, technically called "pleadings" in Anglo-American law (see BOUVIER, LAW DICTIONARY, tit. "Pleading"), and oral persuasion, colloquially called "pleading." Confusion is promoted by the cognation of the English word "pleading" (with its two meanings) and the French plaidoirie (whose technical meaning is oral advocacy).
advocates, and notaries, they may lawfully carry on activities which would be considered the "practice of law" if carried on in the United States.\textsuperscript{135}

There is no doubt that some of these unlicensed counsellors are thoroughly competent, nor that there are some who are not. One can only say that the care which should always be used in selecting a professional adviser is even more vital if an unlicensed one is chosen.

5. WHICH KIND OF LAWYER?

The only professionals whose participation is required by law for a European incorporation are the notaries. They are needed for the execution of articles of a stock company in every country but France;\textsuperscript{136} and they are necessary in France to complete the company organization.\textsuperscript{137} In the formation of limited liability companies they are required in Belgium, Germany, and Italy,\textsuperscript{138} but not in France and Luxembourg.

Experienced European businessmen frequently use no more outside professional service than the law requires. They incorporate without the advice of an advocate, and use a notary only in the situations where the law requires it. They do not consult an advocate, an accountant, or a tax specialist, unless the incorporation presents unusual technical problems.

American investors, on the other hand, have generally consulted European advocates, and obtained through them such services as might be needed from notaries, accountants, and tax specialists. Perhaps this has frequently been done under a belief that an advocate, like an American lawyer, is the only qualified adviser on

\textsuperscript{135} An English solicitor and law teacher, Mr. L. Neville Brown, informs us that in England also "the lawyers' monopoly... has been eaten away as far as counseling in tax and corporation matters is concerned by the professional accountant and various business consultants."

\textsuperscript{136} Belgium: C. Com. I-IX, arts. 29, 31, 33.

\textsuperscript{137} Germany: AktG § 16. The law requires notarial or judicial execution; but notarial is the practical choice.

\textsuperscript{138} Luxembourg: Company Law arts. 26 and 30.

\textsuperscript{139} Netherlands: W.K. art. 36.

\textsuperscript{180} Belgium: C. Com. I-IX art. 4.

\textsuperscript{181} Germany: GmbHG § 2.

\textsuperscript{182} Italy: CODECIVILE art. 2475.
corporate matters. Although such a belief would be false, the practice of consulting an advocate is probably sound. It is safe to say that a European investment by an American enterprise always involves problems which are unfamiliar to the investor. It seems to be the European consensus that the advocate is the professional most likely to have a sound perspective concerning the ensemble of problems likely to arise, and the one best qualified to draw in others' talents.

With this comment we would like to pass on two warnings from our European informants. The American investor should not expect his advocate to produce in his own office all the expertise and the documentation required; he should be prepared to have the advocate draw on other professionals or to send the American to them.

It should also be clear that the American does not always need a European advocate. If he is reliably referred to a French or German notary, it is probable that the notary is just as competent as any advocate to decide when other professional collaboration is called for. Likewise, an American lawyer practising in Europe (without a European license) may be perfectly competent to supply the perspective which is commonly obtained from a European advocate, and to call on the other professionals (notaries, tax specialists) who may be useful.

E. The Organic Documents

I. DRAW THEM IN EUROPE!

The late Professor Ascarelli once remarked that it is of secondary importance whether the American investor asks an advocate, an accountant, or a notary to draw his European articles of incorporation. The thing of primary importance, he said, is this: don't draw the articles in New York and send them to Rome or Hamburg. Not only are such articles invariably far from the demands of local law and practice, but they impose on a European lawyer an impossible job of explaining to the American client why they must be changed. What the American client should send to Rome or Hamburg is a statement of what activities he wants to conduct, where he expects to get his money, whom he expects to employ as managers, and other information on operational plans; the drafting he should leave to the European adviser.

In the light of this advice—which appears to us to be very sound
—there is not much to say on this side of the water about the organic documents. We will offer a few observations designed chiefly to improve communications between transatlantic and cisatlantic lawyers.

2. ARTICLES AND BY-LAWS

One does not, of course, ask a European lawyer to prepare a set of articles and by-laws. The Europeans do not use these two sets of organic documents; their functions are combined in one document. Telling him to draw a set of “articles” may also contain elements of confusion; the more English he knows, the more likely he is to be confused. For instance, he may know that the basic document in Delaware and New York is called the “certificate of incorporation,” and in England (from which many Europeans surprisingly take their English), “memorandum of association.” What then are “articles of incorporation?” It may be helpful to have at hand some European names of the formative documents—acte constitutif, Gründungsvertrag, atto constitutivo, akte van oprichting.

These European names are not the end of the matter, either. We have in America one set of names for the basic document, when we think of it as something signed and filed during the formative process of the corporation; these are “certificate of incorporation” or “articles of incorporation” (varying by jurisdiction). We have another set which we use after the corporation has been fully organized, to refer to the contents of the document, and to include amendments to it; thus we speak of the limitations of the “charter.” Likewise Europeans have a set of names which signify the organic law of the company, as derived from the articles and amendments. The principal terms are statuts, Satzung or Gesellschaftsvertrag, statuti, and statuten.139

Many of the elements found in European articles of incorporation are the same as those in American articles. They indicate the statutory type of company (stock or limited liability), the purpose, the name, the duration, and the amount of capital.140 In all limited

139 Gesellschaftsvertrag is generally applicable to all commercial companies, including stock companies, limited liability companies, and partnerships. Satzung is a special name for the Gesellschaftsvertrag of a stock company (used also for the partnership limited by shares, Kommanditgesellschaft auf Aktien). See, for instance, usage in HUACK, GESELLSCHAFTSRECHT 24, 116 (1958).

140 For the principal statutory sections on contents of the articles of incorporation see the following:

Belgium: C. Com. I-IX, art. 30 (stock companies); arts. 120-121 (limited liability companies).
liability companies, and in stock companies except in France, the incorporators are named in the articles. To the practiced American eye, nothing essential is lacking except that the purpose clause is much shorter.

3. PURPOSE CLAUSES

There are considerable variations in the laws and practices of the various countries with respect to purpose clauses. The law and practice in France is liberal. A popular form book advises the incorporator, after stating the objects which he has in mind, to add as additional objects,

Investment by the company, by any form or means, in any business and any company now existing or which may come into existence.
And all industrial operations in general.\textsuperscript{141}

Professor Houin considers this bad practice, but notes that it is widely followed, and that the undesirable consequences are uncertain.

While this approach will remind an American lawyer of some of the clauses seen in Delaware and other American charters, there is an important difference. One never encounters the three-page list of purposes and powers which are customary in Delaware, and often used in other American states, and any European lawyer would probably resist any suggestion that he imitate it. There are at least two reasons. One is that the law authorizes the articles to state purposes, not powers. The other is that the ultra vires doctrine, whose ravages in the United States brought forth the inflated American purpose clauses, never received such extreme applications in countries of Europe.

Broad purposes clauses are apparently tolerated also in Germany, Italy, and Luxembourg, so long as some real purpose exists.\textsuperscript{142} In two nations—Belgium and the Netherlands—vague or omnibus purpose clauses are inadmissible. The Belgian company law was

\textsuperscript{141} LEMEUNIER, POURQUOI ET COMMENT CONSTITUER UNE SOCIÉTÉ ANONYME p. I–7 (1928).

\textsuperscript{142} Our German collaborator warns that a company might be successfully attacked
amended in 1958 to require a "precise designation of the purpose of the enterprise." In the Netherlands the Ministry of Justice is likely to refuse a permit to incorporate if the declared objects go beyond the potential of the company's capital.

4. RULES OF INTERNAL GOVERNMENT

Any brevity which European articles acquire through the shortness of their purpose clauses is soon lost by the length of their provisions for internal government. The articles contain innumerable details on shareholders' meetings—when they are held, how they are called, who may be admitted, how the agenda is made up, how minutes are kept, how votes are counted. Many of these provisions will be found to restate propositions of the company law of the particular country. These portions of the articles are much like the by-laws of a typical American corporation.

It is obviously inconvenient to have to include all this material in the formally filed articles; it is of no interest to the state, or the creditors, or anyone other than the shareholders. But since there is only one organic document in European company law, these necessary provisions must be put in it.

The burden of including these internal matters in the articles is recognized by some of the publication laws. In France and Germany publication is required only of an extract of the articles; the extract corresponds roughly to American articles, and excludes most of the "by-law" items. In Belgium the extract procedure is used for limited liability companies, but not, unfortunately, for stock

if it were formed without any specific purpose in mind, but merely to serve some later need which might appear; that is Gesellschaft auf Vorrat.


144 France: The extract for the société anonyme requires: (1) type of company (e.g., stock company or limited partnership with shares); (2) name; (3) purpose; (4) central office; (5) names and addresses of members; (6) names of managers and auditors; (7) amount of capital, value of shares, and description of property (if any) exchanged for shares; . . . (9) provisions (if any) for special reserves; (10) whether there are any shares with double vote, or any founders' shares; (11) when the company begins and expires; (12) the court in which the complete articles and other documents were filed. Law of 1867, art. 57. The extract for the SARL is substantially the same. Law of 1925, arts. 13 and 14.

Germany: The extract for the stock company must contain the company name, central office, purpose, date of organization, names of managers, and also (if applicable) any provisions which may exist limiting the duration of the company, or limiting the agency powers of the managers or liquidator, or limiting the "authorized" capital. AktG. § 32. The limited liability company extract is similar. GmbHG § 10. The cited sections refer to the entries in the Commercial Register, but these entries must be published by the court, by virtue of HGB § 10.

145 C. Com. I-IX, art. 7(b). The Belgian publication requirement includes two items
Italy, Luxembourg, and the Netherlands require publication of complete articles in all cases.\textsuperscript{147}

F. Incorporators

One of the striking peculiarities of European incorporation, from an American viewpoint, is the insistence on numerous incorporators. The laws do not generally state a minimum number of signers of the formative documents, but they do specify the minimum number of shareholders, and European lawyers generally conclude that the full benefits of incorporation are not attained until that number of shareholders exists. For stock companies, the minimum number is seven in Belgium, France and Luxembourg,\textsuperscript{148} and five in Germany.\textsuperscript{149} In Italy and the Netherlands two will suffice for a stock company,\textsuperscript{150} and two will do for a limited liability company in all the countries where such a company may be formed.\textsuperscript{151} But no member of the Common Market has followed the example of a few American states which permit a single investor to incorporate.\textsuperscript{152}

Requirements of this sort give little difficulty to an American lawyer on his home grounds; any group of clerks will do for incorporators, and shares can be subscribed and paid for in their names. But many European lawyers will object to this kind of practice. Our Belgian, French, and Dutch collaborators all warn against the unpleasant legal consequences which might result from procedures of this sort; only the German colleague sees no problem.

which would probably be found in American by-laws—the fiscal year, and the date of the annual shareholders' meeting.

\textsuperscript{146} C. Com. I-IX, art. 9.
\textsuperscript{147} Luxembourg: Company Laws art. 8.
\textsuperscript{148} Belgium: C. Com. I-IX, art. 29.
\textsuperscript{149} France: Law of 1867, art. 23.
\textsuperscript{148} Netherlands: W.K. art. 367.
\textsuperscript{150} Luxembourg: Company Law art. 26.
\textsuperscript{151} AktG § 2.
\textsuperscript{152} Italy: Codice Civile art. 2247.

Belgium: C. Com. I-IX, art. 119.
France: Law of 1925, art. 5.
Germany: GmbHG § 2.
Italy: C. Civ. art. 2247.
Luxembourg: Company Law art. 183.
Iowa Code § 491.2 (1958).
Our Luxembourg collaborator, while disapproving the use of straw incorporators, reports that this is the usual thing in foreign-owned companies, especially holding companies.

The precise nature of the dangers incurred by using straw incorporators are not very clear. One of the consequences is said to be liability for losses occasioned by the pretense; but if the straw man's subscription is actually paid, there would seem to be no loss. In Belgium a statute provides that shareholders are liable for debts of the company until the required complement is reached. Our Belgian collaborator warns that the straw man commits a crime by falsely representing himself to be a subscriber, which he is not; but admits that the probability of prosecution is slight.

The most serious probable consequence applies only to the situation in which the various incorporators are all nominees of one investor, so that the new company is in reality a one-man company, or a wholly-owned subsidiary from its very inception. In this situation European theorists (unlike American) are inclined to regard the company as having no legal existence. One theory behind this view is the classic principle of continental law that a company is the result of a contract; and a contract with only one party is just as impossible in European law as in American.

Contemporary European jurists are well aware that the modern company is much more an institutional entity than it is a contract, and a few of them would be willing to discard entirely the contractual view. But the contractual theory is deeply ingrained in the statutory system, and jurists cannot disregard it just because they are tired of it. In the law of France, the law of "associations" (sociétés), which include all kinds of business corporations, as well as partnerships and non-profit organizations, appears in the Civil Code as a subdivision of the law of contract; the French Civil Code's first words on company law are, "An association is a contract. . . ." Many Europeans also adhere to the view, not unheard of in

153 Belgium: Code Com. art. 35.
154 To the same effect, see van Ryn, op. cit. supra note 85, at 496.
155 For a comparison of contractual and institutional concepts, see Hamel and Lagarde, Traité de Droit Commercial 468-469 (France 1954).
156 C. Civ. art. 1832: "La société est un contrat par lequel deux ou plusieurs personnes conviennent de mettre quelque chose en commun dans la vue de partager le bénéfice qui pourra en résulter." This is the first section of Title IX—"of the Contract of Association" (du contrat de société). This title follows titles on sale, exchange, and bailment, and the title on loans. The same conceptual arrangement is met in the civil codes of Belgium and Luxembourg. It is only slightly different in Germany, where we need only substitute the word "obligation" (Schuldverhältnis) for "contract."
America, that the debt-escaping functions of a corporation can be justified only if the corporation also promotes true group activity. For these and other reasons, European theorists are accustomed to say that a company in which there was only one bona fide investor at its inception is a nullity. The theory has been put into effect in various ways. In the Netherlands a series of tax cases attributed company income directly to the company's real owner, whose fellow-incorporator had been a mere nominee for him. In France heirs were allowed to claim the property of a bank incorporated by their ancestor in league with straw co-investors. In Italy a statute which makes a sole shareholder liable for the company debts incurred while he is sole stockholder might be applied to one who holds some of the shares through straw men.

The burden of procuring incorporators who meet European standards will probably not prove very heavy. For ordinary corporations there is no requirement that the incorporators be Europeans; they can be Americans. Neither do they have to be present; they can act by attorney-in-fact. Finally, they do not have to be natural persons; except in a Belgian limited liability company and a French stock company, all the incorporators can be corporations. Hence, an American corporation and one of its American subsidiaries could be the incorporators of a limited liability company in France, Germany, Luxembourg, or Italy, or of a stock company in Italy or the Netherlands. Seven American corporations, or seven corporations and individuals in any combination, could incorporate a stock company in Belgium or Luxembourg. Six American corporations and one individual could form a French stock company.

The test of bona fide investment is also easily met. One of our French informants, who is most positive about the danger of straw men, assures us that there is no danger in taking from each of the other incorporators a written agreement to sell his shares of stock at par on demand. A Dutch decision has held that a company was

---

159 Decision of May 30, 1928, Beslissingen in Belasting Zaken (hereinafter B.) 4279.
160 Decision of April 15, 1931, B.4965.
158 Court of Cassation, decision of May 19, 1926, Dalloz, Recueil Périodique et Critique, I at 25 (France 1929).
160 C. Civil art. 2362.
161 Mr. Bruna, one of our Italian collaborators, states that prevailing Italian opinion permits holding through strawmen, unless there were a subjective intent to escape obligations.
162 There are very few exceptions, such as, in France, petroleum extraction companies, newspaper publishing companies, travel agencies, which must have a majority of French shareholders.
not proved to be invalid merely by evidence that one of the two incorporators sold his shares to the other on the very day of incorporation.\textsuperscript{162}

We do not pretend to appraise the importance of having bona fide incorporators, or the risks of not doing so. We think, however, that the American investor should be prepared for the request that he, not his European lawyer, produce incorporators in the required number, and that each of these incorporators should pay separately his original subscription for shares. We have the impression that most American companies comply with this request, when made; and we think that it is wiser to comply than to become a party to a test case on an unsettled point of European law.

G. CAPITAL AND ITS PAYMENT

I. STATEMENT IN THE ARTICLES

In five of the six Common Market nations the amount of "capital" stated in the articles is quite a different thing from the "authorized capital" which is stated by the articles in most American states. "Authorized capital" means, in America, the amount which may be issued before amending the charter; some of it may not be subscribed for some time to come, and some may never be subscribed. Americans like to have a "cushion" of uncommitted stock to meet unforeseen needs.

In the Common Market (outside the Netherlands) the capital contains no uncommitted cushion. The "capital" means the subscribed capital, and the corporation is not fully organized until the stated amount is 100% subscribed. Some of the statutes say expressly that the company is not perfected until it reaches this point;\textsuperscript{163} even when the statutes are silent, the law is probably the same.

In consequence, the stated capital should be set at an amount for which present subscribers are readily available.

If the incorporators foresee that future capital demands will exceed the amount for which present subscriptions are available, they can sometimes make charter provisions for future increases by

\textsuperscript{162} Decision of the Hooge Raad of Dec. 14, 1932, B.5339.
\textsuperscript{163} Belgium: C. Com. I–IX, art. 29 (2) (stock companies).
France: Law of 1925 art. 7 (limited liability company).
Germany: AktG § 22 (1) (stock companies).
Italy: CÓDICE CIVILE art. 2329 (1) (stock companies).
Luxembourg: Company Law art. 26 (stock companies), art. 183 (limited liability companies).
means simpler than getting a shareholder’s vote on a charter amendment. Italy and Germany permit stock companies to adopt charter clauses which authorize the managers to increase the capital.\textsuperscript{164} But the authorized increase must also be fully subscribed within a limited time—five years in Germany, one in Italy. In this respect, it is quite unlike American “authorized capital.”\textsuperscript{165} France also has some statutory provisions permitting “variable capital,” but they are somewhat inconvenient, and are little used.\textsuperscript{166} Other kinds of companies can increase their initial capital only by charter amendment; this applies to limited liability companies in all five countries, and to stock companies in Belgium and Luxembourg.

The requirement that all capital be subscribed when the company is formed does not imply that it must all be paid in at that time. All the stock company laws specify some minor fraction of the stock which must be paid in; the fraction is 20\% in Belgium and Luxembourg, 25\% in France and Germany, and 30\% in Italy.\textsuperscript{167} The limited liability laws in France and Luxembourg require payment of 100\% of the amount subscribed,\textsuperscript{168} but elsewhere permit the same fractional payments as in stock companies.\textsuperscript{169}

The fractional payment provisions are primarily directed at payments made in money. When shares are to be paid for in property, different rules may apply. French law specifically provides that payment in property must be made in full at the formation of the company,\textsuperscript{170} and the Belgian law is the same.\textsuperscript{171} Elsewhere, the rules

\textsuperscript{164} Germany: AktG § 169; The increase is limited to 50\% of the stock before the increase.

\textsuperscript{165} Italy: Codice Civile art. 2443.

\textsuperscript{166} Law of 1867 arts. 48–52.

\textsuperscript{167} Some of the inconveniences are that the stock cannot be made negotiable, either in bearer or registered form (art. 50), and that members can resign and withdraw their share, or be expelled (art. 52).

\textsuperscript{168} Belgium: C Com. I–IX, art. 32.

\textsuperscript{169} France: Law of 1867 art. 1, para. 2. The balance must be paid within five years.

\textsuperscript{170} Law of March 4, 1943 art. 1.

\textsuperscript{171} Germany: AktG § 28 (2).

\textsuperscript{172} Italy: C. Civ. 2329.

\textsuperscript{173} Luxembourg: Company Law art. 26.

\textsuperscript{174} Germany: GmbHG § 7.

\textsuperscript{175} Italy: C. Civ. art. 2476 (cross-referring to stock company requirements).

\textsuperscript{176} Luxembourg: Company Law art. 183.

\textsuperscript{177} Belgium: C. Com. I–IX, art. 120. However, at least 50,000 francs (about $1000) must be paid in, whatever fraction of the whole it may be.

\textsuperscript{178} Germany: GmbHG § 7.

\textsuperscript{179} Italy: C. Civ. art. 2476 (cross-referring to stock company requirements).

\textsuperscript{180} Law of 1867, art. 4.

\textsuperscript{181} As to limited liability companies, full payment of property contributions is expressly required by C. Com. I–IX, art. 120.
for payments in property are no stricter than for payment in money, and perhaps less so.\textsuperscript{172}

The result of these requirements is that the capital to be stated in the articles should be determined in this way:

in a French, Italian or Luxembourg limited liability company, it should be an amount which known persons are willing immediately to subscribe and pay in full;

in a Belgian, French, German, Italian, or Luxembourg stock company, and in a Belgian or German limited liability company, it should be an amount which known persons are willing immediately to subscribe in full, and pay to the extent of 20 to 30 percent.

In stating the matter in this way, we are greatly oversimplifying the theory. In theory it is possible to have an incorporation “by stages,”\textsuperscript{173} in which incorporators subscribe for part of the capital in the first stage, and then sell the rest of the shares through a public offering; the incorporation is complete at the end of the public offering stage. But this procedure exposes the whole venture to the danger that the public will not subscribe to 100\% of the offered shares; in that event, the incorporation would collapse unless the subscribers consented to a charter amendment. As a practical matter, well advised investors seldom if ever would launch a company in this way. They might seek to avoid the risk by obtaining an investment banker to subscribe for the shares not taken by incorporators; but this stratagem is hardly practicable in a newly formed company.

The situation in the Netherlands is quite different. Only one fifth of the capital stated in the articles needs to be subscribed forthwith, and there is no time limit on subscriptions to the remainder.\textsuperscript{174} Of the fifth subscribed, only one tenth needs to be paid on each subscribed share;\textsuperscript{175} a company could properly carry on business with as

As to stock companies, the requirement of full payment rests on the opinions of commentators. See \textit{van Ryn and Heenen}, \textit{2 Droit Commercial} \textbf{11} (1957).

\textsuperscript{172} See \textit{Godin-Wilhelmi}, \textit{Aktiengesetz} § 28, Anmerkung \textbf{11} (1950).

\textsuperscript{173} Known to French commentators as \textit{fondation successive} and to Germans as \textit{Stufengründung}. Special statutory provisions to deal with the phenomenon are found in the French Law of 1867 art. 4, and in the German AktG § 30.

\textsuperscript{174} Netherlands: W.K. art. 36c. The subscriptions are a prerequisite to issuance of the Certificate of Incorporation, without which companies are forbidden to do business. W.K. art. 36g. If the amount has not been paid in, the board members are individually and jointly liable for all the debts of the enterprise. However, the company can lawfully do business without the payment if the board members are prepared to bear the risk.
little as a fiftieth of the declared capital paid in. The declared capital thus appears to be nearly as flexible as the "authorized capital" of a typical American corporation.

The minimum amounts of declared capital which are required by some of the European company statutes are not likely to deter investors who are prepared to cross the ocean to open a business; the highest are Germany's—about $25,000 for a stock company, and $5000 for a limited liability company.176

2. SHARES OF STOCK; PAR VALUE

Some difficulty in talking about shares in European companies is occasioned by the fact that all the European countries have two terms, where we have only one. While we may speak indifferently of a man's "share" in a partnership, or his "share" in a corporation, the Europeans have one set of terms for a share in a partnership (part, Teil, parte, deelbewijs) and another set (action, Aktie, azione, aandeel) for a share in a stock company. This difference has to be noticed because in connection with the limited liability company Europeans always use the partnership term rather than the stock company term. Hence, the American investor will get a share called a Teil if he invests in a German limited liability company but will get a share called an Aktie if he invests in a German stock company.

This is the European jurists' way of emphasizing that the limited liability company share is non-negotiable, while the stock company share may be negotiable. For purposes of the incorporation process, the two kinds of shares are much alike. Both are normally stated in units of identical value, and the investor acquires a given number of such shares, as in an American corporation, rather than an undivided fraction of the equity, as in an American partnership. He buys 200 out of 1000 shares, not merely a "20% interest."

176 Belgium: No minimum for a stock company; Bfr 50,000 (about $1000) for SPRI, C. Com. I-IX, art. 120.
France: No minimum for stock company.
1,000,000 (old) Ffr (about $2,000) for SARL, Law of 1925 art. 6.
Germany: 100,000 DM for stock company. AktG. § 7.
20,000 DM for GmbH. GmbHG § 5.
Italy: 1,000,000 IL (about $1500) for a stock company. Codice Civile art. 2327; reported due to be increased to 25,000,000 IL (about $40,000). 50,000 IL (about $75) for an SARL. Codice Civile art. 2474; reported due to be increased to 1,500,000 IL (about $2500).
Luxembourg: No minimum for stock company.
1,000,000 Lfr (about $3000) for SARL. Company Law art. 182.
Netherlands: No minimum.
The shares are stated in money values, such as 500 francs or 100 marks, except that Belgium and Luxembourg permit stock companies to issue shares without par value. The other countries do not authorize no-par shares.

In Europe, as in America, shares cannot be issued for less than par, but there is no law against issuing them above par, perhaps ten or twenty times above par. Many European minimum par values are fairly low—for limited liability company shares about $1.50 in Italy, and $10 in France; for stock company shares only $1.00 in Luxembourg. Hence it would be theoretically possible to introduce the "low-par" system in vogue in the United States. However, no one has done so, and we doubt that it would result (as in Delaware) in creating a large "surplus" which would be free of the restriction placed on capital.

3. PAYMENT FOR SHARES—MONEY OR PROPERTY

The Common Market countries have a curious collection of provisions regarding the payment of consideration for shares. They are rather different from any regulations known in the United States, but their origin is not hard to guess. It is evident that the free-booting promoters of the late nineteenth century, there as here, issued themselves shares for which they never paid at all, or for which they paid in property taken at gross over-valuations, with disastrous results for innocent investors and creditors.

There are minimum share values in some countries:
- France: 5000 Ffr (about $10) for SARL, Law of 1925 art. 6.
- Germany: 100 DM (about $25) for AG. AktG § 8.
- Italy: 1000 IL (about $150) for SARL. Codice Civile art. 2474.
- Luxembourg: 50 Lfr (about $1.00) for SA. Company Law art. 37. 500 Lfr (about $10) for SARL. Company Law art. 182.

Belgium: C. Com. I-IX, art. 41.
- Luxembourg: Company Law art. 37.

In the Netherlands, this is expressly provided, subject to the exception that the underwriter may receive a discount of 6%; W.K. art. 38a. In other countries, this rule is not expressly stated, as in many American corporation laws, but results from the requirement that the stated capital must be 100% subscribed. See note 163, supra.

Liberty to sell for more than par is specifically granted in German stock companies. See AktG §9(2).

German stock company law requires that any premium over par value be stated in the publicly filed documents of organization (AktG. §§ 16(2) and 28(2)), and that the premium should form part of a legal reserve which is not available for dividends (AktG § 130).

Italian law requires that premiums should not be disbursed until a reserve equal to one-fifth of the stated capital is accumulated from earnings (C. Civ. 2430), but apparently permits disbursement after that time.
To these evils American courts responded, as we know, with doctrines making subscribers liable for any deficiency in the value of consideration received for their shares.\textsuperscript{183} Later, legislatures reacted with Blue Sky laws, designed to enable government officials to determine whether the initial investments in the company had been duly made.\textsuperscript{184} European courts responded in different ways, and their responses explain some of the regulations on payment for shares. For cash payments there are regulations of special interest in French, German, and Italian stock companies, which concern the 25 or 30 percent of the stock subscriptions which must be paid in at or before the completion of incorporation. In France and Italy they must be deposited in a bank, or with a notary, where they are not available to the company and its promoters until the incorporation is complete in every respect.\textsuperscript{185} Presumably these safeguards are designed to guarantee to creditors that the minimum capital has actually been paid in; or perhaps to guarantee to shareholders that their fellow shareholders have also made a proportionate contribution. In Germany they do not have to be banked, but if they are, the bank must certify that the deposits are unrestricted.\textsuperscript{186}

For the payment of subscriptions in property, the special regulations are more complicated and more widespread. In the first place, payments in property may have to be 100\% paid in the course of incorporation; in France and Belgium the payments on account which are sometimes permissible for cash subscriptions are inadmissible for subscriptions payable in property.\textsuperscript{187}

Second, the property which is to be exchanged for stock must, in many instances, be stated in the articles, so that every other incorporator knows about it, and every creditor can learn about it. This is the rule in Belgium, Germany and Luxembourg both for stock companies and for limited liability companies.\textsuperscript{188} It is the rule

\textsuperscript{183} Scovill v. Thayer, 105 U.S. 143, 26 L. Ed. 968 (1881); Stevens, Handbook on the Law of Private Corporations § 183 (1949); Ballantine on Corporations §§ 343 ff. (1947).

\textsuperscript{184} Loss and Cowett, Blue Sky Law 1–10 (1958); Loss, Securities Regulation 7–16 (1951).

\textsuperscript{185} France: Law of 1867, art. 1; the funds must be deposited in the official national depositary—Caisse des Dépôts et Consignations—or with a notary.

\textsuperscript{186} Italy: Codice Civile art. 2329; the payments must be made to a special account in any bank.

\textsuperscript{187} AktG §§ 28(2), 29(1).

\textsuperscript{188} Belgium: C. Com. I–IX, art. 30 (stock company), art. 121 (limited liability company).

Germany: AktG § 20; GmbHG § 5(4).
for limited liability companies in France,189 and for stock companies in the Netherlands.190

A third regulation sometimes encountered is a requirement of appraisal, the most complicated plan for which is met in the French stock company.191 After the stock has been subscribed, a first meeting of subscribers is held, at which auditors are appointed. The meeting is adjourned, the auditors appraise the property, and a second subscribers' meeting is held to hear and to accept or reject the auditors' report. At this meeting, if the property transfer is approved, permanent officers may be elected, and the incorporation completed. In German stock companies, there is no second organization meeting, but independent auditors must be appointed to value the property, and the company must not do business until after the appraisal is made and reported to the court.192 In Italian companies of both types, a court-appointed auditor makes the appraisal which is attached to the incorporation papers; after the company is organized, the elected directors and auditors must review the appraisal.193

A fourth precaution of the legislator is to impede transfer of the shares received for property. In French stock companies such shares cannot be represented by certificates, and hence are non-negotiable for two years after incorporation;194 in Belgium and Luxembourg they are not freely negotiable for approximately two years;195 in Italy they are non-transferable until the directors and auditors have made the post-incorporation appraisal.196

A fifth hazard is reserved for the property-subscribers in a French limited liability company.197 Instead of having an appraisal

---

189 Law of 1925, art. 8.
190 W.K. art. 40a. Netherlands, of course, has no limited liability companies.
191 Law of 1867, art. 4.
192 AktG §§ 25, 26, 34.
193 Codice Civile art. 2343 (stock companies), art. 2426 (limited liability companies). Deficiency in the value of the assets does not avoid the formation of the company, but merely requires a reduction in the stock allotted to the subscriber, and consequent reduction of the company's stated capital, unless the subscriber pays up the deficiency in money. The subscriber may elect to withdraw entirely, resulting in a still greater reduction in the stated capital.
194 Law of 1867, art. 3(5).
195 Belgium: C. Com. I-IX, art. 47. The shares can be transferred, but only if they are in registered form, and the transfer is made with specified formalities.
196 Luxembourg: Company Law art. 44.
197 Codice Civile art. 2343; the code declares the shares inalienable (inalienabili) during this period.
198 Law of 1925, art. 8.
at the incorporation stage, the subscribers are made jointly liable to the company's creditors for any deficiency which may later appear to have existed between the value of the contributed property and the par value of the shares. Only when ten years have passed is this threat lifted.

These various regulations are not only burdensome; they are also rather fearsome beartraps, since any failure to comply may result in some sort of invalidity of the corporation, or liability of the incorporators, or both. The French legislator, in particular, seems to have prepared ambuscades for any little businessman who might think of turning his business over to a corporation in exchange for a portion of the shares.

This situation calls for careful study by the American corporation which plans to establish subsidiaries in Europe. If the subsidiary has been preceded by any sort of operations in the area, the parent will be expecting to contribute money and property which was used in the pre-incorporation business. And if no thought were given to the matter, these assets would naturally be transferred in exchange for stock.

If the resulting formalities are found, on investigation, to be insufferable, there is sometimes a way of avoiding them. Imagine, for instance, an American corporation which was planning to transfer its stock of goods and intangibles, with its current bank account, to a forthcoming French subsidiary. Imagine further that the parent corporation planned to loan the subsidiary additional funds which might be useful in further development.

The parent can greatly simplify its problem by reversing the roles of property and cash. Instead of contributing property and loaning cash, it can contribute cash and loan property. That is, it may buy shares for cash, and transfer the property on a deferred payment plan. The financial risk is the same (assuming the amounts are equal), but the juridical risks which result from the special incorporation formalities are escaped. There may be some new formalities to be observed in regard to interested directors; but these are less burdensome.

In Germany this simple reversal of roles would not help much. There the special formalities which apply to exchanges of stock for property also apply to property purchases contemplated at the time of incorporation,\(^{198}\) or made within two years thereafter.\(^{199}\)

\(^{198}\) AktG § 20. See also § 45—purchases of property amounting to one-tenth of the corporate capital.

\(^{199}\) AktG. § 45.
H. FILING AND APPROVAL

The procedures do not usually involve long waits for administrative action. In all the Common Market countries except the Netherlands, the ancient theory that incorporation is a privilege to be granted at the sovereign’s discretion was discarded decades ago. For local citizens, incorporation is a matter of right; when the correct formalities have been executed, the papers deposited, there is nothing to wait for.

Even for foreigners, there are no administrative waits in connection with ordinary incorporations. Under international law they can lawfully be excluded from incorporation if they are not the beneficiaries of treaties of friendship, commerce, and navigation; but in fact they are not excluded. They do indeed encounter administrative obstacles in getting licenses to be merchants or corporate executives, or in getting licenses to exchange money for the purpose of investment, or in getting licenses to enter certain trades. But these obstacles are not connected with incorporation procedure.

In the Netherlands incorporation is not a matter of right, either for citizens or for foreigners. It is a privilege granted at the discretion of the Ministry of Justice. In considering whether to grant an application, the Ministry will consider all kinds of factors—whether the industry will further complicate an over-supply of goods or services, whether it will hurt or help the Netherlands’ foreign exchange position, whether the proposed capital is adequate, and whether the financing plans offer any threat to the investment market. Presumably, a wise investor will explore all these matters before preparing incorporation papers. If major policy questions have been cleared in advance, less than a month will usually be required to obtain approval of the application to incorporate.

IV. MANAGEMENT OF A EUROPEAN SUBSIDIARY

The most elusive problem in all companies everywhere is probably management. If the right men can be given the right powers, they will solve the other problems. In foreign subsidiaries the problem is naturally complicated by different languages and different conceptions of teamwork, as well as by the special ambiguities of a subsidiary position.

200 The principal exceptions are (1) specially regulated types of enterprise, such as banks and insurance companies; (2) enterprises in which foreign participation is limited, such as (in France) petroleum extraction and newspaper publication.
In attacking these problems an American lawyer will need some conception of the legal structures of management in European countries, and some appreciation of how they differ from American legal structures.

A. THE PARALLEL ORGANS OF MANAGEMENT

The European corporate scene presents a surprising variety of organs of management. None of the organs corresponds exactly to American institutions, and the similarities in names are often more misleading than enlightening. Before we can discuss (in the English language) the European institutions, we will have to explain the European institutions which we are designating by our English terms.

1. SHAREHOLDERS

In Europe, as in the United States, we start logically with the holders of ultimate power—the shareholders. In Europe a sharp distinction is often drawn between holders of the normally negotiable shares of stock companies (who are called actionnaires, Aktionäre, soci or aandehouders) and holders of the non-negotiable shares of limited liability companies and partnerships (who are called associés, Gesellschafter, soci, or vennooten). Since we have no such choice of terms in America, we will have to use the word "shareholders" to designate the holders of both types of European shares.

2. GOVERNING BOARD

After the "shareholders," the most important title in the American corporate hierarchy is the "directors," and one is naturally tempted to search for the European institution which can be fairly translated by the same term.

The search is doomed to failure. The first problem is a linguistic one. The Europeans have corporate officials called by a name which looks like "director,"—directeur, Direktor, or dirretore—but they are in many ways the opposites of American directors. While the ordinary American "director" is almost always elected by the shareholders, the European directeur, Direktor, or dirretore, is never so elected. While the American title implies a deliberative, part-time

201 Typical of the provisions indicated is the Delaware provision, "The business of every corporation . . . shall be managed by a board of directors, except as hereinafter or in its certificate of incorporation otherwise provided." 8 DEL. CODE § 141 (1953).
position, the European title implies an executive, full-time position. While the American title implies a position on the highest hierarchical level (after the shareholders) the European title implies subjection to a superior board. Consequently, it is best to avoid entirely the word "director" in referring to European corporate officials.

When we turn from names to substance, the problem is still baffling. There are commonly not one, but two, boards which divide the functions of management and control. In the face of this duality, we can speak collectively of European boards only by making an arbitrary classification which achieves consistency on one plane at the price of inconsistency on another.

In the discussion which follows, we will adopt the name of "governing board" for that board which resembles the American board of directors in that (1) it is chosen by the shareholders and (2) it chooses other executives and managers to perform subordinate functions. This is the conseil d'administration in France and in French-speaking Belgium and Luxembourg, the Aufsichtsrat in Germany, the consiglio d'amministrazione in Italy, the Verwaltung in German-speaking Luxembourg, the raad van bestuur in Netherlands, and the raad van beheer in Flemish-speaking Belgium. The members of this board are variously known as administrateurs, Aufsichtsratsmitglieder, amministratori, Verwalter, bestuurder, and beheerder.

This board is not the only group chosen directly by the shareholders, for the same is true of the auditors (commissaires aux comptes, Bilanzprüfer, sindaci, commissarissen). Neither is it the only group which may name subordinate executives; in Germany, at least, this may be done by another board, the Vorstand. But it is the only group which is both chosen by the shareholders, and invested with authority to name managerial officers.

3. EXECUTIVES

Successful European companies, like their American counterparts, generally have a chief executive in whom all reins of authority are concentrated. We need not pause over a rare exception like the great Italian Montecatini Company, which concentrates executive power in two men of equal authority, like the ancient Roman consuls.

However, we must avoid assuming that the executive power is held by the presiding officer of the governing board, as it usually is in the United States. Although a European governing board usually elects a president, the presidency of that board signifies something
more like being an American "chairman of the board" than being an American "president." There are other titles which we will translate as "general manager" (directeur général, direttore generale, algemen bestuurder, algemen beheerder, and occasionally General­direktor) and "managing director" (administrateur délégué) which signify the concentration of executive power. Even in France, where the president is required by law to assume responsibility for the company's management, he has the choice of delegating the authority to a subordinate general manager, or exercising it himself under the compound title of "president and general manager" (président-directeur-général).

In Germany, the president of the "governing board" (that is, the board elected by the shareholders) is forbidden to be an executive; the executive power must be wielded by a subordinate board (the Vorstand), or its president (German stock companies having two boards and possibly two presidents).

There is also the possibility of having an executive officer elected directly by the shareholders, with no intervention of any board at all; this is possible in limited liability companies in all countries, and in stock companies of Belgium, Italy, and Luxembourg.

Hence we will speak of "executives" to designate those functionaries who hold the reins of authority under any of a great variety of titles, and by any of a great variety of methods of appointment.

4. AUDITORS

While American corporation laws leave directors free to choose the auditors of their books, European laws commonly provide formally for the election of officials to review the accounts and the performance of the management. The titles of most of these officials would be literally translated as "commissar"—commissaire, Kommissar (in Luxembourg), commissaris. Since this word would probably evoke in most American readers visions of Stalinist agents, we will call these officials "auditors."

5. CONTROL

One other word which we cannot help using requires a little explanation. We will use "control" in the sense which has become fairly standard in America through Berle and Means' Modern Corporation and the rules of the Securities and Exchange Com-

---

202 The German and Italian terms—Bilanzprüfer and sindaci—are less misleading.
mission;\textsuperscript{204} we use it to mean the ability to exercise a decisive influence on the management of the company—the relation which the U.S. government contended (and the companies denied) existed between General Motors and du Pont de Nemours.\textsuperscript{205}

We mention this only because the cognate European words (\textit{contrôle}, \textit{Kontrolle}, \textit{controllo}) are usually used in the more limited sense of the power to inspect accounts and review operations.\textsuperscript{206} This meaning is reflected in the American office of "controller," and is sometimes met in English-language discussions of foreign company law; it will not be used here.

For convenience of reference, on pages 92–93 we offer a table of English terms which we will use, and the indigenous names of the various institutions to which we will be referring.

B. MAJOR DIFFERENCES IN EUROPEAN MANAGEMENT STRUCTURE

The difficulty of naming the officials in European management reflects much deeper differences in their roles. We will sketch some of the more obvious differences, and show how an American investor may take advantage of these differences or, at least, minimize their inconveniences.

I. SUPREMACY OF THE SHAREHOLDERS

A striking peculiarity of European management structures is the power of the shareholders in the statutory plan. The legislator has not designed them to be a mere electoral college, to choose the leadership to which the company shall be entrusted. The shareholders are generally the supreme governing body, and the governing board is merely their agent, responsive to their will. Even in Germany, where the reforms of 1937 were intended to give increased independence to the executive board,\textsuperscript{207} the shareholders have distinctly greater powers than are usual in the United States. This conception expresses itself in many ways, such as the rule that dividends must be declared or at least confirmed by the shareholders rather than by the governing board alone, as in America.

\textsuperscript{204} See \textit{Loss, Securities Regulation} 453 ff. (1951).
\textsuperscript{208} See \textit{Berle, Jr., Control in Corporation Law}, 58 Colum. L. Rev. 1212 (1958); "Control may be defined as the ability to choose directors."
\textsuperscript{200} Cf. \textit{van Ryn} who equates \textit{contrôle} with "a mission to determine the necessary facts (about the management) and report the results to the shareholders." (This author's translation.) \textit{Principes de Droit Commercial} 416 (Belgium 1954).
\textsuperscript{209} \textit{Hueck, Gesellschaftsrecht}, 125, 126 (Germany 1958).
\textsuperscript{206} Belgium: C. Com. I–IX, art. 79 (right to adopt financial statement in stock companies); art. 137 (same in limited liability companies). (Continued on p. 94)
<table>
<thead>
<tr>
<th>Country and Language</th>
<th>Shares</th>
<th>Shareholders</th>
<th>Meeting</th>
<th>Governing Board</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium-French</td>
<td>actions</td>
<td>aandelen</td>
<td>vaaotenen</td>
<td>conseil d'adminISTRATION</td>
</tr>
<tr>
<td>France</td>
<td>parts</td>
<td>actionnaires</td>
<td>assosées</td>
<td>algemene vergadering</td>
</tr>
<tr>
<td>Germany</td>
<td>Anteile</td>
<td>soci</td>
<td>parts</td>
<td>Aktionäer</td>
</tr>
<tr>
<td>Italy</td>
<td>quote</td>
<td>azioni</td>
<td>parts</td>
<td>Aktionäer</td>
</tr>
<tr>
<td>Luxembourg-French</td>
<td>actions</td>
<td>associs</td>
<td>assemblée générale</td>
<td>Gesellschaft</td>
</tr>
<tr>
<td>Luxembourg-German</td>
<td>Anteile</td>
<td>Aktionäer</td>
<td>associs</td>
<td>Gesellschaft</td>
</tr>
<tr>
<td>Netherlands</td>
<td>aandelen</td>
<td>aandelhouders</td>
<td>algemene vergadering</td>
<td>raad van bestuur</td>
</tr>
<tr>
<td>Country and Language</td>
<td>Member of Governing Board</td>
<td>General Manager</td>
<td>Departmental Manager</td>
<td>Manager (in limited liability co.)</td>
</tr>
<tr>
<td>----------------------</td>
<td>---------------------------</td>
<td>-----------------</td>
<td>---------------------</td>
<td>-------------------------------</td>
</tr>
<tr>
<td>Belgium-French</td>
<td>administrateur</td>
<td>directeur</td>
<td>directeur</td>
<td>gérant</td>
</tr>
<tr>
<td>Belgium-Flemish</td>
<td>beheerder</td>
<td>algemen</td>
<td>bestuurder</td>
<td>zaakvoerder</td>
</tr>
<tr>
<td>France</td>
<td>administrateur</td>
<td>directeur général</td>
<td>directeur</td>
<td>gérant</td>
</tr>
<tr>
<td>Germany</td>
<td>Aufsichtsrat-mitglied</td>
<td>—</td>
<td>Direktor</td>
<td>Geschäftsführer</td>
</tr>
<tr>
<td>Italy</td>
<td>amministratore</td>
<td>direttore</td>
<td>direttore</td>
<td>amministratore sindaci</td>
</tr>
<tr>
<td>Luxembourg-French</td>
<td>administrateur</td>
<td>directeur général</td>
<td>directeur</td>
<td>gérant</td>
</tr>
<tr>
<td>Luxembourg-German</td>
<td>Verwalter</td>
<td>General-direktor</td>
<td>Direktor</td>
<td>Geschäftsführer</td>
</tr>
<tr>
<td>Netherlands</td>
<td>bestuurder</td>
<td>algemen</td>
<td>bestuurder</td>
<td>—</td>
</tr>
</tbody>
</table>
The most important aspect of shareholder supremacy is the power to remove top management, which may be stated as a general principle of European company law, subject to some qualifications. Even in French limited liability companies, where the statute declares that the managers are never removable without cause during their terms, case law sanctions reservation in the articles of a power of removal. A qualification must be noted in Germany, where the shareholders' removal power affects the highest board (Aufsichtsrat) but not the subordinate executive board (Vorstand). In some limited liability companies, managers who are named in the articles of incorporation are removable only for cause or as provided in the articles (or an amendment of them). Subject to these limited exceptions, European shareholders have the power to remove the board members without cause.

Another kind of qualification must be noted in Belgian and Luxembourg stock companies. Although the shareholders as a group are supreme, no one shareholder is allowed to vote more than two-fifths of the votes cast at any meeting, nor more than one-fifth of the outstanding shares. An American parent company owning 99% of a Belgian subsidiary's stock might therefore find itself unable to oust a management, if the other 1% were held by the managers to be ousted. This eventuality should be foreseen and sidestepped by dividing the 99% between the parent and two other subsidiaries.

The shareholders' supremacy means a great deal to American

---

France: Hamel, Traité de Droit Commercial no. 720 (1954); in limited liability companies, the manager may determine the dividends himself; id., no. 812.
Germany: AktG § 126; GmbHG § 46(1).
Italy: Codice Civile art. 2433 (stock companies); art. 2492 (limited liability companies).
Luxembourg: Company Law art. 75 (stock companies); Cf. art. 197, para. 5 (limited liability companies).

209 AktG. §§ 75(3), 87(3). A commentator suggests that a shareholders' vote of no confidence in the executive board might be "cause" for removing them. Godin-Wilhelmi, Aktiengesetz § 75, Anmerkung 7. But the decision would lie with the Aufsichtsrat.
211 Belgium: C. Civ. I-IX, art. 53 (stock companies).
France: Law of 1867, art. 22 (stock companies).
Germany: AktG § 87(3); GmbHG § 38 (limited liability companies).
Italy: Codice Civile art. 2383 (stock companies; removal subject to member's right to damages); art. 2487 (limited liability companies same as stock companies).
Netherlands: W.K. art. 48b.
212 Luxembourg: Company Law art. 71(2).
Belgium: C. Com. I-IX, art. 76.
parents of European subsidiaries and offers an escape from a prevailing dilemma. On their first entry into Europe, American parent companies are faced with the alternative of staffing the subsidiary with Americans, who do not know much about Europe, or with Europeans whom the parent company does not know much about. The parents are understandably apprehensive of the possibility of runaway policies of European managers, because they do not know the Europeans' personal qualities so well, and they sense that their European employees are not so tightly tied as Americans would be to the parent company. In consequence, one finds many European governing boards in which a majority of seats has been reserved for Americans who can make only short and fleeting visits to Europe.

This reservation of a safe majority would be quite essential in an American corporation, where removal of directors is seldom provided for by statute and is generally presumed to be permissible only for cause. It is generally unnecessary in Europe, where the governing board of managers can be removed without any cause as quickly as a shareholders' meeting can be called. The hasty trans-Atlantic flights of American board members to make up a European company quorum are largely unnecessary. A single proxy-holder for a majority of the stock, living in Europe and keeping himself informed of the actions of the European board, could assure the board of immediate dismissal if they should disregard parent company wishes. This device is used successfully by at least one experienced American corporation in Europe.

Shareholder supremacy is also important to an American company which is buying control of a European company. When making a similar purchase of an American subsidiary, it would possibly bargain for resignations of the incumbent directors, so that it could make its newly acquired control effective. Such bargaining is unknown and unnecessary in most European companies because the power to dismiss the governing board or managers comes automatically with the ownership of shares.

2. ONE-MAN MANAGEMENT

A second major distinction of European management is the legality of one-man management, as opposed to the three-man board which comprises the usual minimum tolerated by American corporation statutes. Although one-man managements sometimes exist in U.S. practice, they exist only because no one bothers to en-
force the law requiring the election of additional directors, and their participation in management.

In Europe, on the other hand, one-man management is specifically authorized for limited liability companies in all countries, and impliedly permitted even in the stock companies of Italy and the Netherlands.

The sole manager option was doubtless designed, at least in limited liability companies, to permit the incorporation of business enterprises which formerly had been sole proprietorships, and where the investors concurred in a desire to keep the same man at the helm. This may also be the reason why some laws facilitate the irremovability of the manager.

The convenience of one-man management for a company which is new in Europe is evident. An American investor may enter the European market with very slight acquaintance among European businessmen. If he does not have more than one American employee whom he wishes to keep in Europe, or no more than one European whom he trusts to run his business, he would have difficulty in naming a three-man board. Fortunately, he does not need three men. He can give all powers to the one man he trusts, until longer acquaintance enables him to broaden the managerial base with confidence.

The investor who takes this option must, of course, watch out for other risks. The one-man management may be irremovable except on proof of misconduct or incompetence unless proper reservations have been made in the articles of incorporation. In addition to this, there are legal provisions which give the manager almost unlimited authority to bind the company. Finally, there is the human danger that one head will make mistakes which three heads would have avoided.

214 Belgium: C. Com. I-IX, art. 129.
Germany: GmbH § 6.
Italy: Codice Civile art. 2487.
Luxembourg: Company Law art. 191.
215 No number is specified by these stock company statutes:
Italy: Codice Civile art. 2380.
Netherlands: W.K. art. 472.
In one sense, one-man management is permitted by the German stock company law, since the executive board (Vorstand) may have only one member. But since there must be a three-man supervisory board (Aufsichtsrat) above him, this is not the kind of one-man management which simplifies a parent company’s personnel problems.
216 See notes 209, 210, 211 supra.
217, 218 See notes 209, 210, and 211 supra.
219 In Belgium, France, and Luxembourg, the manager of a limited liability com-
3. ONE-COMPANY MANAGEMENT

Even more surprising from the American point of view is the rule which permits one company to occupy a position as manager, or governing board member, in another. Statutes forbid a company's filling certain positions, such as president of a French stock company, or any managerial office in a German company; the interpretation of prevailing legal opinion is to a similar effect in Italy. European lawyers believe that managerial positions in the Benelux countries, and positions other than president in France can be filled by an artificial person as well as by a natural one.

Hence, the possibility arises of appointing another European company—perhaps an affiliated one—as sole manager of a European subsidiary. Of course, such an arrangement should be only temporary. As a matter of practical psychology, it is a good idea to have a board of living men with a lively interest in the company and sense of responsibility toward it. But the use of an incorporated manager may bridge difficult initial gaps. Since the corporate manager can appoint anyone it wishes to act as its human agent, the problem of managerial tenure is side-stepped.

4. GOVERNING BOARDS AND EXECUTIVES

We have already mentioned two peculiarities of European governing boards—the fact that in some kinds of companies there need not be a board and that, if there is one, its members can be removed at the unfettered will of the shareholders. A third peculiarity of European boards is that, with a few exceptions, the board members may act as a joint executive. They do not need to act through officers; they may, by virtue of their positions, act to negotiate and sign contracts. In short, most of the European laws make no provisions for the separation of policy-making and executive functions which are basic to American thinking about management structure.

In small enterprises this may be all to the good. Many American writers have been suggesting that we should in America provide for boardless management in "close corporations," and have cited Eu-
European experience to support their contention. But it is obvious that larger concerns need a plural board, with a systematic delegation of executive functions.

The significance of this state of affairs for the American investor is that in many European company forms he may and he must create the management structure that his business requires. The law does not furnish him a pattern into which he must fit. If he wants a one-man management, he can probably have it. If he wants a governing board, with a president, secretary, and treasurer, his lawyers will have to draw the articles of association so as to provide for them.

We will now deal with some of the exceptions to the general rule—exceptions which impose some standard pattern of organization on the European company. These mandatory patterns are found in the stock companies of Italy, France, and Germany.

The Italian law of stock companies requires the election of a president (presidente), but nothing is said about his powers or responsibilities; the delegation of executive functions is therefore as unfettered as anywhere else. If the president is to have power to make contracts of purchase, sale, and employment, the articles of incorporation should say so. There are no requirements for a secretary or treasurer, and such officials are never used in purely Italian companies. American owned companies can and often do name such officials, but there is no great merit in the practice since the offices have no meaning for the Italians who deal with the company, and probably very little even for the Italians who fill the offices.

In France, the law has caught up with good business practice. It not only requires that each stock company have a three-member board, but also requires that the board elect a president, and that the president assume responsibility for the management of the company. Other board members must refrain from exercising executive functions unless they are appointed to them. The president may be the general manager or may appoint someone else to the job, but he is responsible for the management in either event.

The qualifications of board members and of the president are specific but not particularly onerous. The board members may not occupy similar positions in more than seven other French companies. The president cannot be simultaneously president of more

---

222 C. Civ. art. 2380. The president may be elected by shareholders but if they fail to do so, he is chosen by his colleagues on the board.
223 Law of Nov. 16, 1940, art. 1-2; Law of March 4, 1943, art. 14.
224 Ibid.
225 Law of Nov. 16, 1940, art. 3, as amended by Law of July 7, 1953.
than two companies; but since the statutory office of president exists only in stock companies, this rule seems not to inhibit his serving as a manager of a limited liability company, or as a managing partner in a partnership. The president must be a natural person, but there is no rule against the other board members being companies.

These provisions of French law were adopted by the "collaborationist" government at Vichy, while northern France was occupied by Germany during World War II. They were precipitated by the disruption of management resulting from the division of the country by enemy occupation and the absence of board members who were either prisoners of war in Germany or with the outlawed Free French forces in Africa. The promulgation of these provisions as separate laws rather than amendments to the company law probably reflected the legislators' conception of them as emergency legislation, rather than permanent reform.

Probably no one wants a return to the amorphous pre-war law, but the present provisions are widely regarded as poorly designed. Dean Hamel of the Paris law faculty has written, with characteristic irony,

> The law of 1940 gave companies a choice of two formulae,—that of the president-and-general-manager, or that of the nonexecutive president who is liable for the acts of his general manager. Several commentators thought they detected here a reflection of the German law of 1937, and of the famous *Führer-Prinzip*. The president was to be the head-man of the stock company. He does indeed occupy a fine position in the statutory text; but what a peculiar head-man—who can be removed at pleasure by his peers (the other board members), and even indirectly by the shareholders; whose powers depend on the authority which the board has given him, and can at any time amend. The president has only one characteristic of a head-man—increased liability. This feature is his best argument in deliberations, and it does increase his influence, if he knows how to use it.

What the law expresses is primarily the desire to put a stop to the parceling out of responsibilities between the president and the managing director, or worse, among several managing directors or general managers. It has concentrated responsibility on the president. That way, there is always someone to hold responsible.

---

226 Law of Nov. 16, 1940, art. 3.
5. THE GERMAN BOARDS

The organization of management in German stock companies is so distinctive that it calls for a special description. There are normally two boards, instead of one, which might be called “governing,” and which divide between them the features and the functions of an American board of directors.

The one which we have grouped with other “governing boards” in the preceding discussion is more accurately called the “supervisory board” (Aufsichtsrat; literally, “board of oversight”). It resembles the American board of directors in that a majority of its members is elected by the shareholders, and in that it in turn elects the executives. It differs from an American board of directors in that its decisions do not bind the company in dealings with outsiders, but it does make binding decisions to hire and fire executives and set their pay; it elects the executives from persons who are not its own members; and its members include labor representatives, who must comprise one-third of the board’s membership.

The other German board we will call the “executive board,” although its German name (Vorstand) apparently signifies something like “chairmanship” (literally, “those standing in front”). It resembles an American board of directors in that its decisions bind the company to outsiders, that its president, if any, is the chief executive of the company, and that each of its members is usually known as a Direktor. It differs from an American board of directors in that its members are not elected by the shareholders, but by the supervisory board; it is not necessarily a plural board, but may consist of only one man; if plural, it cannot elect its own

228 AktG §§ 70, 86.
229 Id. § 87(1).
230 Id. § 75(1).
231 The statute provides that “conduct of business (Massnahmen der Geschäftsführung) cannot be taken over by the supervisory board.” AktG § 95(5).
232 AktG § 75.
233 Id. §§ 77, 97.
234 Id. § 90(1).
236 AktG § 71.
237 At least, he holds the power of decision (AktG § 70(2)), although he does not automatically gain authority to deal with outsiders (§ 71(2)).
238 By prevailing practice, not law.
239 AktG § 75(1).
240 Id. § 70(2).
Organizing for Business

101

President but must await the supervisory board’s decision as to whether there should be one and, if so, who he shall be; if the board has a president, the other members cannot overrule him, but can be overruled by him; its members are rarely outsiders, because they cannot be at the same time managing officers or general partners in any other commercial business.

In the presence of these diversities, it seems futile to debate whether the American board of directors is more like the German supervisory board or the German executive board. The discussion would be like that of the blind men around the elephant. It would be further complicated by the fact that American boards are so disparate—some of them consisting largely of outsiders who review the executives’ work, others consisting entirely of insiders, who carry on the work of the company under the guiding hand of the president. The former type of board is more like the German supervisory board; the latter type, more like the German executive board.

For an American enterprise which is first entering Germany, the staffing of the two boards presents problems. The supervisory board is a powerful group in which one would want to place only trusted and competent persons, but the persons must be “outsiders,” holding no managerial office in the enterprise. Such persons are not easily found.

The choice of the executive board members also appears to be a very serious matter. Like most American directors, and unlike governing board members in some other countries, the German executive board members cannot be removed except for “good cause.” The executive board’s power to bind the corporation to outsiders cannot be limited by charter provisions.

The problem of choosing members for the two German boards cannot be evaded by naming another company as a board member;

241 Id. § 75(2).
242 Id. § 70(2).
243 Id. § 79(1).
244 See Baker, Directors and Their Functions, 11–27 (1945).
245 “Good cause” is not defined in the statute. Various commentators suggested soon after adoption of the statute that “good cause” might include such matters as a non-confidence vote by the shareholders, but the Federal Supreme Court has warned that such a vote would not be “good cause” if it were based on insubstantial grounds, or if it were adopted merely for the purpose of justifying the executive’s dismissal. Decision of Apr. 28, 1954, Bundesgerichtshof (II Zivilsenat) 13 Entscheidungen des Bundesgerichtshofes in Zivilsachen (hereinafter cited as BGHZ) 188, at 193.
246 AktG. § 74(2). There is some dispute as to the effect of limitations on an outsider who has actual knowledge of them. Hueck, Gesellschaftsrecht 130 (1958).
the law specifically excludes this. The best one can do is to reduce the necessary number to one by incorporating in the limited liability company form, instead of the stock company. A limited liability company does not need to have a supervisory board unless it has 500 or more employees.

Although the German two-board system is undeniably complex, it is not necessarily a system to be shunned. A distinguished Belgian writer compares it favorably with the Belgian system. German companies seem to have the reputation of being very well managed, and we think the system presents more advantages than obstacles to a company which is well-established, and which has ample resources of managerial man-power. But the system must be frankly regarded as burdensome for small, new companies, and probably contributes to the fact that limited liability companies are preferred to stock companies more frequently in Germany than in any other Common Market country.

6. LABOR PARTICIPATION IN MANAGEMENT;
CO-DETERMINATION

In Europe as in the United States, the last decades have seen a phenomenal growth in the rights of labor representatives to influence the decisions of management. But the European developments have taken different forms from those which we have seen in North America.

One of the principal developments in Europe has been the labor-management councils, where representatives of labor and management meet together to discuss and resolve problems affecting both. These are not like American collective bargaining sessions, at which plenipotentiaries trade commitments binding each side to the other. They are more in the nature of forums at which representatives of each side try to persuade those of the other that it would be best for all parties if the other side's desires were met.

This institution has gone furthest in Germany, with its celebrated "co-determination." This term is coupled with another to make the title of Part IV of the German Plant Management Law of 1952—Cooperation and Codetermination (Mitwirkung and Mitbestimmung). Every business establishment (subject to a few exemptions)

247 Id. § 75(1)—executive board § 86(2).
248 BetrVerfG § 77.
249 Van Ryn, op. cit. supra note 6, at 381, 382.
250 BetrVerfG, see note 48 supra.
has to have a plant council, elected by the employees. They consult with the management on nearly every phase of operation. Their orbit includes specifically "group interests" (soziale Angelegenheiten) such as working hours, pay periods, and vacations, and "individual interests" (personelle Angelegenheiten), such as hiring, firing, transfers, and promotions. Workers in larger enterprises also consult indirectly on "business matters," which embrace manufacturing methods, the production program, the financial status of the business, and market conditions. For these matters, there is an "economic committee" (Wirtschaftsausschuss) composed of at least four members named by management and four named by the plant council.

The capstone of the German program is representation of labor in the supervisory board. One-third of the supervising board members are elected by the employees. That leaves two-thirds to be chosen by the shareholders; of these, one-third may be appointed by particular shareholders specified in the charter, while only one-third is required to be elected by the general body of shareholders. But usually the body of shareholders elects two-thirds.

The representation of employees in the supervisory board applies only to companies which have a supervisory board on which the employees can be represented. For this very purpose, the law of limited liability companies was amended in 1952 to require that they, too, should have supervisory boards, if their employees exceed 500. On the other hand, stock companies with fewer than 500 employees are exempted from the requirement if they are "family companies," owned entirely by one person or by a small group of closely related persons. Hence, employees have to be represented today on the boards of all non-family stock companies, and on the boards of limited liability companies which have more than 500 employees.

But exemption from board representation does not imply exemption from other phases of "co-operation and co-determination."
It is difficult to say whether the influence of employees in Germany is due chiefly to the plant councils alone (the Betriebsräte), or to the joint economic committees (Wirtschaftsausschussen), or to representation on the supervisory board. Many companies which escape the requirement of labor representation on the supervisory board must still establish plant councils or joint economic committees or both.

France also has a law designed to enlarge the voice of labor in company management, dating from 1945, a few months after liberation. This law provides for "enterprise committees" which consist of the chief officer of management and a delegation of worker representatives varying according to the number of employees to be represented. The enterprise committee is authorized to express its opinions on all questions which effect the organization of the business, or the distribution of profits; and has rights to be consulted on all matters affecting the management of the business, and its progress, and to receive the same financial statements which are given to shareholders. In stock companies, two labor representatives have the right to attend governing board meetings, with a right to speak but not to vote.

According to our information, the voice of labor in German industry has been a good deal stronger than in France. We are told that French enterprise committees concern themselves chiefly with the pay and working conditions of the employees, while German employee representatives exercise a considerable influence on decisions affecting production.

In neither country do employee representatives dictate to company executives. Much less do they participate in the executive functions of management. The most that can be said is that in certain classes of German companies, employee representatives hold the balance of power in the election of executives when any substantial division arises among the shareholders' representatives.

In other Common Market countries, as in the United States, employee representation is less formalized, but employers are obliged by legal or extra-legal pressures to listen to their employee's desires and complaints. Luxembourg law provides for employee "delegations" to consult with management in the larger enterprises. In

261 Ordinance of Feb. 22, 1945, instituting the "comités d'entreprises."
262 Id. art. 3.
263 See AktG § 95(5), forbidding members of the governing board to take over conduct of the business (Massnahmen der Geschäftsführung).
Italy, "internal commissions" with consultative powers are commonly set up by collective bargaining agreements.

7. QUALIFICATIONS OF BOARD MEMBERS: NATIONALITY AND STOCKHOLDING

The laws of European countries are generally very liberal with respect to who may be members of the governing boards of companies. In two countries—France and Belgium—prior conviction of various heinous crimes will disqualify. In France, some or all of the board members must be French nationals in local railroad companies, hydroelectric companies, public utility companies, petroleum production companies, and companies formed for mining in French colonies. In the Netherlands, a proportion of a shipping company governing board must be Dutchmen in order to permit the company to fly the Dutch flag. And in both French and Belgian companies, members of the governing board must obtain a "merchant's license." In France this is said to be obtainable by any foreign businessman who has no criminal or bankruptcy record; in Belgium it is said to be more exceptional. Aside from these requirements, European boards may legally be composed partly or wholly of Americans.

Only in French stock companies is it required that the board members be shareholders. In both French and Italian stock companies there are requirements that shares be deposited as security for the potential liability of the board members; in France these shares must be registered in the names of the members whose good conduct they secure. This probably means that the French board members should be beneficial shareholders; but in practice, "quali-
fying shares" are transferred by the real owner into the name of the French board member. In Italy, shares are deposited for the non-owning board member without even putting them in his name.

The choice between foreign (American) or local (European) board members must be based less on legal than on practical considerations. We have encountered companies with the greatest variation in practice. One successful company with many foreign subsidiaries followed the practice of having the same three Americans serve as president, secretary, and treasurer, and also as directors, of more than a dozen foreign companies; they were also a majority of the board in most cases. At the other extreme, we have found subsidiary companies which take pride in having a board of exclusively "local" personnel. On examination of the facts, we sometimes found that some of the "all-French" boards were American citizens, but they were at least permanent residents of France.

Choices in these matters must depend on many factors, of which the foremost will be how many local people the investors know well enough to trust their integrity, ability, and judgment. But we wish to register the observation that the companies with the longest and most successful experience in foreign countries are those which tend most strongly to compose their boards exclusively of local residents, of whom a majority are local citizens.

This policy is not to be confused with that of permitting participation of local capital. Many of the companies which have gone the farthest in engaging local management are strictest in regard to holding substantially all the shares.

The reasons for employing local management are not based on apprehensions of hostility to Americans. So far as we can determine, neither banks nor regulatory agencies have any hostility to American managers. The main reason is that Europeans can do the job better. They are better guessers about the psychology of European buyers, sellers, laborers, and landlords. They are also better analysts of the objectives and the standards of European bankers who must lend money, and of the European officials who must grant permits and licenses. Their advantage in this respect cannot be bought from them in consultations as effectively as it can be evoked by giving them the responsibility for decision.

A second reason for employing local management is cost. We start from the fact that, in terms of official exchange rates, American salaries are higher for comparable jobs than are European. Europeans may live just as well or better on their nominally lower
salaries; but Americans going to Europe will demand the nominal equivalent of their American salaries, plus overseas benefits and travel expenses which will make their total cost about twice the cost of Europeans. A bull market for European managerial talent is reported to be narrowing the gap; but it will remain substantial.

Hence, we are inclined to believe that every investor in a European subsidiary should aim to reach the point where his entire governing board and executive personnel are European residents.

8. AUDITORS

The position of auditor in European companies is quite unlike anything known to the American corporation. Auditors in these countries are not mere outsiders hired by the board to report to it; they are officials of the company, elected by the shareholders to report on the managers. They are seldom optional; they are generally required by law.

Auditors are required for stock companies in Belgium, France, Germany, Luxembourg, and Italy; in some of these countries they are also required for certain limited liability companies. In the Netherlands, where auditors are not required by statute, they may be imposed by the company’s own articles, and frequently are.

The various European legislatures have entrusted to their company auditors functions of varying scopes, but all of them are much broader than the functions of auditors in the United States. Stock company auditors in Belgium, France, Italy, and Luxembourg have

---

267 We use the term “auditor” for the following European company officials:
Belgium: “commissaires, commissarissen.”
France: “commissaires” in stock companies; members of “conseils de surveillance” in limited liability companies.
Germany: “Jahresabschlussprüfer” in stock companies, “Bilanzprüfer” in limited liability companies.
Italy: “sindaci,” or members of “collegio sindacale.”
Luxembourg: “commissaires” or “Kommissäre” in stock companies; members of “conseil de surveillance” or “Aufsichtsrat” in limited liability companies.
Netherlands: “commissarissen.”

268 Belgium: C. Com. I–IX, art. 64.
France: Law of 1867, art. 32.
Germany: AktG § 135(1).
Luxembourg: Company Law art. 61.

269 France: Law of 1925, art. 32 (over twenty shareholders).
Italy: CODICE CIVILE art. 2488 (capital over one million lire—about $1500).
Luxembourg: Company Law art. 200 (over twenty-five shareholders).

270 W.K. art. 50.
authority to call shareholders' meetings, and those in Luxembourg have "the unlimited power of supervision and inspection of all operations of the company." The title of "supervisory board" (conseil de surveillance, Aufsichtsrat) borne by limited liability company auditors in France and Luxembourg suggests the breadth of their authority. In Italy, the auditors are obliged to attend all shareholders' and governing board meetings, and to investigate shareholders' complaints against the management, and are liable along with board members for company losses which their due care should have prevented.

In spite of these extended powers, the auditors are not in the line of command, as are the organs which we have called "governing boards." The decisive difference between them and the governing boards is their lack of power to choose the executives who run the company.

Although auditors have been required in stock companies for many years, they have not always been very effective. Professor van Ryn of Brussels wrote of the Belgian situation before the legislation of 1953:

As for the auditors, the situation is still more peculiar (than for the governing board); nearly everyone agrees that they never, or hardly ever, effectively do the job of investigation (contrôle) which is their only excuse for existing. The job of auditor is generally a moderately lucrative sinecure, or a waiting room at the entrance of the governing board.

---

271 Belgium: C. Com. I–IX, art. 73.
France: Law of 1867, art. 32.
Italy: Codice Civile art. 2367 (implication).
Luxembourg: Company Law art. 70.
The absence of a similar power in German auditors is probably explained by the grant of a similar power to the governing board (Aufsichtsrat), which is presumed to be as independent of management as the auditors.
271a Company Law art. 62.
272 France: Law of 1925, art. 32 (limited liability companies). Stock company auditors in France exercise a much narrower authority.
Luxembourg: Company Law art. 200 (limited liability companies).
273 C. Civ. art. 2405.
274 C. Civ. art. 2408.
275 C. Civ. art. 2407.
276 See A. A. Berle, "Control in Corporate Law, 58 Colum. L. Rev. 1212 (1958); "Control" may be defined as the capacity to choose directors. As a corollary, it carries capacity to influence the board of directors and possibly to dominate it.
277 Van Ryn, 1 Principes de Droit Commercial 382 (1953). See also Van Ryn, La Réforme du Contrôle des Sociétés Commerciales et l'Expérience Anglaise (Belgium 1945).
Similar remarks could probably have been made in France before 1935.\textsuperscript{278}

To eliminate subservience to the management, most of the countries now have laws designed to assure that the auditors will be completely independent. With some variations among countries, they are disqualified if they are employed by the company, or by the managers of the company, or by affiliated companies, and if they are related by blood or marriage to managers of the company which they audit.\textsuperscript{278}

In Italy the law attempts to insure independence still further by giving the auditors tenure for at least a three-year term unless cause can be shown for their removal, and requiring that their pay be fixed in advance of their term.\textsuperscript{280} In other countries the auditors' tenure apparently remains subject to the will of the shareholders, even though they are elected for various terms ranging from three to six years.\textsuperscript{281}

There are also provisions in some countries requiring that the auditors be qualified accountants. Germany now requires that all auditors be certified public accountants.\textsuperscript{282} In Belgium and France at least one of the auditors must be a certified public accountant in stock companies which have offered their shares to the general public.\textsuperscript{283} In Italian stock companies, at least one and sometimes two of the auditors must be certified.\textsuperscript{284} On the other hand, French limited

\textsuperscript{278} The Belgian company laws in the Commercial Code were amended in 1953 to tighten the auditing requirements. French laws had been revised in 1935 to assure independence of the auditors.

\textsuperscript{279} Belgium: C. Com. I–IX, art. 64, as amended in 1953.
France: Law of 1867, art. 33.
Germany: AktG § 137; there are no interdictions here on relationship by blood or marriage.

Italy: CODICE CIVILE 2399; auditors are also disqualified by a prior bankruptcy, or certain criminal offenses.
Luxembourg: Has no statutory disqualifications.

\textsuperscript{280} C. Civ. arts. 2400, 2402.

\textsuperscript{281} Belgium: C. Com. I–IX, art. 64 bis (expressly removable at will of shareholders).
France: Law of 1867, art. 32 (provides 3 year term but is silent on tenure).
Germany: AktG. § 136(1) and (6).
Luxembourg: Company Law art. 61 (expressly removable at will).

\textsuperscript{282} AktG § 137 (öffentlich bestellte Wirtschaftsprüfer oder Wirtschaftsprüfungs­gesellschaften).

\textsuperscript{283} France: Law of 1867, art. 33 (dans les sociétés par actions faisant appel à l’épargne public).
Belgium: C. Com. I–IX, art. 64 bis, 2 (dans les sociétés ayant fait ou faisant appel à l’épargne public).

\textsuperscript{284} CODICE CIVILE art. 2397; the requirement depends partly on the number of auditors (3 or 5) and partly on the capital (over or under 5 million lire).
liability company auditors are required to be shareholders, which makes it unlikely that they will be experts. Luxembourg and the Netherlands make no statutory requirements for either type of company.

To the American investor in a European subsidiary, the audit requirements will not seem very burdensome, but the naming of auditors for a term of years will call for some study, even though the appointment is revocable. A single auditor is all the law requires except for the requirement of shareholder-auditors in French limited liability companies, and a five-man requirement wherever auditors are needed in Italy. In Germany the appointee may be a qualified auditing firm, rather than an individual. Since the auditors' functions are supervisory rather than executive, qualified accountants can be safely named, even though they know nothing of the company's methods and objectives.

9. COMPENSATION OF BOARD MEMBERS AND EXECUTIVES

In Europe, as in the United States, a variety of systems of payment are in common use—fees for attendance at meetings, fixed salaries and profit shares. The only common form of American compensation which is never encountered in Europe is the stock-option.

The stock option seems to hold no attractions for Europeans. Whether it would have any tax advantage, as it does in the United States, is dubious; at least there are no special provisions favoring it. There are many obstacles to its introduction. In the first place, many kinds of companies are forbidden to have authorized and unissued shares, or to hold treasury shares, against which the options could be allowed. Furthermore, most controlling stockholders in Europe are extremely jealous of their voting percentages, so that they would not be prone to issue new shares changing them. This jealousy is even more marked among American owners of stock in European subsidiaries, so that they would be much less willing to issue stock options in their European subsidiaries than they would in the parent companies. Mandatory preemptive rights, which give every shareholder a right to subscribe proportionately to new shares, would be an additional obstacle. The cumulation of obstacles to

285 Law of 1925, art. 32.
286 Codice Civile art. 2397. The law says that the auditing board (collegio sindacale) may have either three or five members; but in either case, there must be two substitute members.
287 AktG § 137.
stock option compensation in Europe leads us to exclude it from further consideration.

In Europe, as in the United States, there are procedural problems in awarding compensation to governing board members, because of the conflict of interest involved in payments by the board to itself. As any American lawyer would expect, one way out is to submit the compensation arrangements to the shareholders for their approval, and this is expressly permitted by statutes in Italy and the Netherlands. But the American usage of inscribing the compensation plan in the by-laws cannot be used since there are no by-laws. Instead, we find many European compensation provisions in company charters.

There is no necessity for shareholder action, or inclusion in the charter, where there is no conflict of interest. For instance, the German supervisory board can fix the compensation of the executive board. In France the governing board can fix the salaries of the president and of the general manager (whether the jobs are separate or combined), and can award compensation to other board members for specific services. Furthermore, when the shareholders have fixed the fraction of the profits which the board members may receive, the board members decide how to distribute it among themselves.

A second problem is the percentage of the profits which can be awarded as compensation. In French stock companies this is limited to 10 percent. In German stock companies, it is limited more generally to an amount which is "reasonably related to the expenditures made for the benefit of subordinate personnel, or for the common good." The public prosecutor is empowered to take action if this vague standard is violated, and the Minister of Justice may issue regulations to make it more specific. In both France and Germany the statutes require the setting aside of proper reserves before the profit shares are calculated.

The deduction of profit shares in calculating taxable income is severely limited. In Italy they are never deductible. In France and

---

288 Italy: Codice Civile art. 2389 (stock companies), 2487 (limited liability companies).
Netherlands: W.K. art. 48c.
289 This is expressly authorized by the Italian and Netherlands statutes cited in the preceding note, and in Germany, AktG § 98(1). The Italian law (C. Civ. 2389) permits the articles to authorize the governing board to fix the compensations of those members who have particular duties (cariche particolari)—a very vague phase.
290 Law of March 4, 1943, art. 11.
291 Ibid.
292 See the immediately preceding citations.
Luxembourg a distinction is drawn between profit shares paid to the executive member of the board (pré­sident in France, adm­in­­is­trateur délégué in Luxembourg), and to other members. The profit shares of the former are deductible; the other members' shares are not. As a consequence, profit shares are seldom awarded to non-executive board members; they are compensated in meeting fees, or salaries, which can be used to reduce the company’s taxes.

There are other fine distinctions in the French taxation of executive compensation, which determine whether the compensation is taxed to the recipient at the basic rate of 5% or 22%. Only one of these is worth mentioning in relation to over-all planning. In the French limited liability company, a distinction is drawn between “majority managers,” and “minority managers.” The “majority managers” are those who hold a majority of the company stock, and their salaries are taxed at a higher basic rate, presumably on the suspicion that the salaries may be interchangeable with dividends. The tax can be escaped by turning the company into a stock company, where the same distinction is not applied. This difference has led to the common statement among French lawyers that the limited liability company is disadvantageous, from a tax point of view. This observation may be true for individual Frenchmen, but it will not be true for American parent corporations, which we presume will not wish to become the managers of French subsidiaries.

10. CIVIL LIABILITIES OF MANAGERS AND BOARD MEMBERS

The same duties which lie on American officers and directors to manage the business with reasonable care and skill fall on the shoulders of European managers and governing board members, and the same civil liability to indemnify the company or the unpaid creditors for the losses caused by these officials’ sins of omission and commission.293

The law of France offers a very interesting addition to this burden. If a stock company becomes bankrupt, the trustee in the bankruptcy may petition the court to saddle the board members not

293 Belgium: C. Com. I–IX, art. 62 (stock companies), art. 132 (limited liability companies).
France: Law of 1867, art. 44 (stock companies); Law of 1925, art. 25 (limited liability companies).
Germany: AktG § 84 (executive board), § 99 (governing board); GmbHG § 43.
Italy: CODICE CIVILE, arts. 2392 (stock companies), 2487 (limited liability companies).
Luxembourg: Company Law art. 59 (stock companies), 192 (limited liability companies).
Netherlands: W.K. art. 47 c–d.
only with the losses traceable to their own conduct, but with all the
debts of the company. Apparently, the trustee needs to present no
evidence in support of his petition; the burden is on the president
and the other board members to prove that they applied "the energy
and the diligence of a full-time employee to the management of the
company's business." 294

This unusual provision was another of the innovations of the
Vichy régime. In an interesting case decided in 1951, the Court of
Commerce for the Seine made each of the non-executive board mem-
bers liable for 5% of the total company debts, and three persons who
had served as president liable for 15%, 15%, and 35%, respectively.295

Like some other Vichy embroideries on the fabric of company
law, this one seems to be accepted as a permanent addition; the
principle was extended in 1953 to French limited liability com-
panies.296 But it does not seem to have spread to other countries.

V. FINANCING A EUROPEAN SUBSIDIARY

A. Monetary Problems

Every investment in European facilities will involve difficult
choices between inside and outside sources of money. By "inside,"
we mean sources of money existing in the same country in which the
facilities are to exist. "Outside" is more inclusive, because it may
include (a) sources outside the country of investment but inside the
Common Market, (b) sources which are outside the Market, but
still inside Europe, or (c) sources outside the European continent.
To be more concrete, a factory in France might be financed from
the "inside" by French funds, or from the "outside" by funds from
Belgium or Switzerland, or the United States.

I. THE LICENSING OF FOREIGN EXCHANGE
TRANSACTIONS 297

As we write these lines, early in 1960, foreign exchange control
laws are still in effect in all the Six Common Market countries. This

294 Law of Nov. 16, 1940, art. 4.
295 Decision of January 19, 1957, Tribunal de Commerce de la Seine (1951), 1 Gazette
de Palais 239.
296 Law of 1925, art. 25, as amended by Decree-Law of August 9, 1953.
297 This subject is more fully explained in Chapter IV supra—"Foreign Exchange
Controls in France," by M. Fernand Jeantet. See also Frank W. Swacker, The Free
Movement of Capital within the Common Market, 15 BUS. LAW. 565 (1960).
means that a governmental agency—which we will call the "exchange control"—has power to forbid any foreign exchange transaction. If a French factory is to be built with money not now in France, the exchange control may by issuing an order (or refusing a license) forbid the purchase of French francs to build it. If the factory has been already built with foreign capital, the exchange control may by like means forbid the owner to turn his French profits into foreign currency in order to repay the foreign investor.

In practice, the Draconian powers of the exchange control are exercised in ways which are generally very favorable to foreign capitalists. In Belgium and Luxembourg, there is today a "general license" for all foreign capital investments; the foreign investor does not even have to get permission before investing, or before repatriating profits and capital. In France, which is currently the strictest of the Six in exchange control, a license is required both for original investment and for repatriation, but is now readily obtained. The license procedure survives chiefly in order to let the government assure itself that Frenchmen are not exporting their own capital (which they are still forbidden to do), and that capital movements are not made for illegal purposes (like supporting the Algerian rebellion).

The survival of the foreign exchange laws and (in some countries) of the licensing procedures also serves to remind the American investor that the present ease of investment and disinvestment is not necessarily a permanent feature of the European scene. Although the history of exchange control in Europe since 1945 is a story of progressive relaxation, there have been periods of renewed restriction as well as periods of relaxation; if future currency crises occur, they are likely to be accompanied by revivals of exchange restrictions.

Some protection against the effect of future restrictions may be obtained by obtaining from the exchange control agency a guarantee of the right to repatriate earnings and capital. In France, where a license to invest is still required, the control agency has an announced policy of permitting repatriation of licensed capital investments and of the profits produced by them. In Belgium and Luxembourg, where no license is required, the exchange control agency may on request give a special guarantee of future repatriation. In Italy, the control agency will guarantee repatriation of capital and unlimited earnings from investments which are deemed
particularly beneficial to the Italian economy, but only capital and earnings at 8% on other investments.\textsuperscript{298}

In addition to the guarantee of repatriability which may be obtained from the exchange control agency, the investor may be interested in examining the guarantees which result from treaty obligations of the European powers. As a part of the plan to unify their economies, the Common Market countries have undertaken to "coordinate" their exchange controls with respect to the outside world, including the United States.\textsuperscript{299} This presumably means some increase in the strictness of controls in the countries which are now "wide open," and some relaxation in countries now strict. The objective is not an arithmetic average, as in the case of customs, but "the highest possible degree of liberalization."\textsuperscript{300} This presumably means the highest degree on which agreement can be obtained; and the agreement must be unanimous, before directives may issue.

Thus it appears likely, as Mr. Jeantet's essay reveals,\textsuperscript{301} that differences between the strictness of the exchange controls which the various European countries apply to Americans and other outsiders may persist at least through the 1960's. Some will license investment and disinvestment very readily, and consistently. Others, with less stable currencies, may be more strict. To complicate the matter, the more strict countries will probably have waves of liberality, when they attempt to emulate the permissive habits of their neighbors, but will later retreat to longer or shorter periods in which repatriation of capital, or even of profits, is restricted.

These probabilities affect the financing plans of American enterprises in two ways. First, the prospect of a liberal foreign exchange policy in any given country increases the attractiveness of investing there; it decreases the risk that the investment will become temporarily or permanently unproductive of American dollars. Second, the prospect of restrictions on repatriation increases the importance of minimizing the investment of outside funds (\textit{e.g.}, dollars) and of maximizing the use of inside funds (\textit{e.g.}, French francs). Even though the parent company has no shortage of money to invest, it

\textsuperscript{298} Law No. 43 of Feb. 7, 1956, and Presidential Decree No. 758 of July 6, 1956. The investments which benefit from the unlimited guarantee are those called "productive," which are generally characterized by the purchase of tangible fixed assets. See Banco di Roma, \textit{I Foreign Private Enterprise in Italy} 23-27 (2nd ed. 1959).

\textsuperscript{299} Treaty art. 70.

\textsuperscript{300} Ibid.

\textsuperscript{301} Supra, note 297.
may wisely refrain from placing more than necessary in a country from which repatriation may prove difficult.

2. TREATY LIMITATIONS ON EXCHANGE CONTROLS

When and if currency controls are revived, inhibiting the repatriation from European countries of American capital and profits, Americans may notice that the controls are not erected against all equally; Americans may be unable to repatriate while residents of countries in the Organization for European Economic Cooperation (O.E.E.C.), and residents of Common Market countries, are less handicapped.

With respect to their fellow members in the O.E.E.C., each of the Common Market countries is somewhat limited in the extent to which it may restrict currency exchanges. The O.E.E.C. includes not only the six Common Market countries but also twelve others, including the "Outer Seven"; of these, England and Switzerland are of particular interest as possible bases of operation for American enterprise. At this writing, the United States is not a member.

In 1953, the O.E.E.C. added to the Code of Liberalisation provisions by which the seventeen members bound themselves to each other to relax reciprocally their exchange restrictions on "invisible transactions," including, among other things, the following items:

- Participation by subsidiary companies and branches in overhead expenses of parent companies situated abroad and vice versa ...
- Dividends and shares in profits.
- Contractual amortization (with the exception of transfers in connection with amortization having the character either of anticipated repayments or of the discharge of accumulated arrears).

With respect to all of these, the eighteen countries of the O.E.E.C. bind themselves to license transfers made pursuant to

---

302 There are currently in process negotiations for a reorganization of the O.E.E.C. which would include the United States and Canada as full members.

303 The Code is strictly speaking a "decision" of the Council of the O.E.E.C., adopted in two official languages (English and French), and known in these languages as "Code de Libération" and "Code of Liberalisation." The original code, adopted in 1950, dealt only with quotas on goods.

304 These items are identified in Appendix B of the Code by reference numbers Ch. I, B/7; Ch. II, B/1; Ch. III, B/2. They are only three out of several dozen kinds of "invisible transactions," so-called in contradistinction to "visible" international shipments of goods. Other invisible transactions include payment for ocean freight, repairs, liability for damages, travel, wages, royalties, etc.
prior licensed undertakings. If a Swiss investment in France was made in 1947 under an exchange license, France undertakes to license payments of the interest and dividends which may become due as a result of that licensed investment. However, the Code of Liberalisation enunciates no policies on the licensing of original investments which may give rise to future overhead expenses, dividends, interest or amortization. As to that, the member countries are presently free to choose. The Organization might conceivably broaden the Code to require freedom of investment among members; but this would require unanimous consent, and looks unlikely.

Among Member Countries of the Common Market, currency controls are much further reduced. In the matter of “current payments” (on account of interest and dividends), all restrictions among member countries are to be lifted by the end of the first stage—that is, presumably by the end of 1961. Since current payments on licensed investments were already freed under the Code of Liberalisation, this provision promises an advance only in that it is not limited to current payments on investments which may have antedated the imposition of exchange controls.

What is more important, the Member Countries bind themselves to abolish by 1970, to the extent necessary for the proper functioning of the Common Market, “restrictions on the movement of capital belonging to persons resident in Member States.” This means new investments. Legislative power to effect this end is given to the Council of the Community, which acquires the right to legislate by majority vote at the end of the second stage (December 1964). By 1970 money accumulated in a Belgian enterprise (for instance) can be invested in France to the extent that a majority of the Community Council thinks appropriate. To be sure, there are escape clauses permitting suspension of the liberties promised; but they are subject to decision of the Council of the Community.

---

306 At present, the growth of the activities and powers of the O.E.E.C. seems to be arrested by the diversion of the leading powers’ interest to the “Common Market” and the “Outer Seven.”
307 Treaty art. 67(2).
308 Treaty art. 67(1).
309 Treaty art. 69. For the kind of “majority” required for this and other legislative acts, see Mr. Stein’s study in this symposium.
310 Under art. 73 (2) a state may on the ground of urgency take unilateral measures to arrest “disturbances in the capital market,” but the Commission of the Community must be informed, and may modify or abolish the measures unilaterally taken.
As a matter of historic fact, the privilege of free investment by a national of one Member Country in another, which was promised for 1970, has already been granted in 1960. On May 11, 1960, the Community Council issued its Directive Number One on the subject of exchange control. It declared that nationals of one state were free to invest in another by purchase of operating properties (investissements directs), by purchase of securities which are traded on stock exchanges, and by purchase of new security offerings, and by various other financial means.

We will try to turn these principles into examples. An American company which wishes to form a French subsidiary must first get a permit to buy francs, and must later get further permits to turn its francs back into dollars to pay interest or repay capital. Currently, both permits may be readily obtained, but the permit to invest might become much harder to obtain on any slight change in the international financial climate; similar circumstances are likely to close down on permits to repay capital. Permits to pay interest and dividends to Americans are likely to survive until a severe crisis; but they enjoy no express treaty protection, and may be expected to be sacrificed before the permits to pay interest and dividends to other European countries—co-members of the O.E.E.C., or of the E.E.C., with whom France has treaty obligations to maintain freedom of exchange.

The position of a Swiss company is slightly better. As to permits to pay dividends and interest, it has the protection of the provisions of the Code of Liberalisation. As to permits to invest or withdraw capital, it is no better off than a Delaware corporation.

The position of a Belgian company is radically different. Procedurally, it has the advantage that there is an executive organ of the Community charged with issuing orders ("directives") to carry out the reciprocal liberalization to which the Member States are pledged. Substantively, it is guaranteed, after 1969, such freedom

---

311 Various Treaties of Commerce, Friendship and Navigation, or of Establishment, promise Americans equal rights with nationals, and rights equal to those of the most favored nation, in regard to exchange control. But since exchange control laws are generally most restrictive on nationals, and do not let them take out any profits except for special requirements, there is nothing to be desired about "national treatment."

The most-favored-nation clause will raise a more difficult question, when and if the Community Council exercises its powers to relay controls on capital movements between Member Countries. However, it is clear that European officials regard the Community as creating an exception to the most favored nation clause. Although American diplomats may argue to the contrary, we will consider this question on the basis of the law as it is now interpreted by the officials who apply and enforce it.

312 Treaty, art. 69.
to invest in France and in other countries of the market, and to withdraw its investments, as the Community Council decrees. That guarantee has already been put (revocably) into effect.

The marked advantages of a Belgian investor in the European market, and the lesser advantages of a Swiss investor, suggest the question whether a Belgian or Swiss company can qualify for the same advantages when it is American-owned. We have already noted that European law regards a company as a national of the country where it keeps its main office; hence one might fairly expect French exchange control officials to give O.E.E.C. treatment to all companies with home offices in Switzerland, regardless of who owns them. But there is one well-known exception to this view of nationality; in respect to seizure of "enemy property," French courts, like American, have recognized ultimate ownership of voting stock as the determinative criterion of nationality rather than location of the home office. That is, a German-owned Swiss company is German under the laws on enemy property. French writers, describing this phenomenon, have referred to the home office test of nationality as the "private law test," and to the ultimate ownership test as the "public law test." Since exchange control is undoubtedly a matter of "public law," the distinct possibility appears that American ownership would prevent a Swiss-based company from claiming the advantages of the Code of Liberalisation. This danger is particularly great in France, where the "control" test of corporate nationality attained great popularity, and was applied to deny foreign-owned companies any compensation for war damages, and even the protection of the new concept of "commercial property." If we think of a Belgian subsidiary instead of a Swiss one, the effect of American ownership involves various provisions of the Treaty of Rome. In Article 58, the control test of company nationality is clearly rejected. It provides,

Companies constituted in accordance with the law of a Member State and having their registered office, central management or main establishment within the Community

---

313 RABEL, 2 THE CONFLICT OF LAWS, A COMPARATIVE STUDY, 57 (1947). This view, which was rejected in the United States following World War I, (Behn, Meyer & Co., v. Miller 266 U.S. 457 (1925)), was adopted after World War II (Clark v. Uebersee Finanz-Korporation 332 U.S. 480 (1947)).
314 ESCARRA, TRAITÉ THÉORIQUE ET PRATIQUE DE DROIT COMMERCIAL No. 63 (1950).
shall, for the purposes of applying the provisions of this Chapter, be assimilated to natural persons being nationals of Member States.

But the article contains the tell-tale words, "for purposes of applying the provisions of this Chapter," and the article is found in Chapter 2, entitled "Right of Establishment." "Establishment" is defined as including "the right to engage in and carry on non-wage-earning activities, and also to set up and manage enterprises . . . subject to the provisions of the Chapter relating to capital." 316 The "movement of capital" is the subject of another Chapter.317 Thus the Treaty clearly differentiates between "establishment" and "movement of capital." 318

We have spoken so far in terms of bona fide Belgian (or Dutch, or Luxembourgeois, or German) companies, owned by Americans, which might wish to expand their operations, or reinvest their profits, in operations in another country (such as France or Italy). If such Belgian companies prove to be free from the exchange restrictions which confront direct American investments, some American would probably attempt to form a Belgian company which had no real Belgian activity, but was formed only to gain entry to France.

In response to any such scheme, France would have a clear right under the treaty to take preventive measures. The Treaty expressly provides that if residents of one Member State makes use of "transfer facilities within the Community . . . in order to evade the rules of one of the Member States in regard to third countries," the Member State may take appropriate counter measures.319 It must consult the other Member States before acting, but does not

316 Treaty art. 52 § 2.
317 Chapter 4, entitled "Capital," comprises articles 67-73, of which the first provides that "Member States shall, in the course of the transitional period and to the extent necessary for the proper functioning of the Common Market, progressively abolish as between themselves restrictions on the movement of capital belonging to persons resident in Member States . . . ."
318 Chapter 2, Right of Establishment, and Chapter 4, Capital, are both parts of Title III, The Free Movement of Persons, Services, and Capital. But there are notable differences in the applicable provisions. Establishment is to be freed without qualification (art. 52) but capital movements are to be freed "to the extent necessary for the proper functioning of the Common Market." (art. 67(1)). On matters of establishment, the Council can act by majority vote after the end of the first stage (art. 54(2)), but on matters of capital movements only after the end of the second stage (art. 69).

However, M. Jeantet seems, in his discussion of "Probable Evolution under the E.E.C. Treaty," to believe that "investments" are entitled to the freedom promised by article 52 to "establishment." (See Chapter IV supra.)
319 Treaty art. 70(2), par. 1.
need to get their agreement; the Community Council can later annul the action, but only on finding that it went "beyond what is required." 320

With respect to freedom of capital movement, the right which each Common Market country guarantees to the others is a right of "movement of capital belonging to persons in Member States" without "any discriminatory treatment based on nationality." 321

The most obvious interpretation of this clause would be that Belgian companies would have freedom to invest in France (to the extent decreed by the Council) regardless of the ownership of their shares. It is not difficult to conjure up an opposing argument, to the effect that if the Belgian company belongs to Americans, its capital is not capital belonging to Belgians; but this argument is likely to be resisted by most of the Common Market members, and French officials might encounter some difficulty in determining just who owns the Belgian company anyway.

Our conclusion is that if France, for instance, should revert to a regime of severe exchange restrictions, companies situated in other Common Market countries (for instance, Belgium) would be much more favorably situated to effect currency exchanges than would Swiss-based or U.S.-based companies. The French might attempt special restrictions on Belgian companies which are owned by non-members of the Common Market; but their attempts to do so would confront practical problems in determining the facts of ownership, and legal problems as to their right to discriminate among Belgian companies based on their ownership. Some of the legal obstacles would be based on the Rome Treaty provisions which we have discussed above; others might be based on various treaties, especially treaties of friendship, commerce and navigation, which we have not mentioned.

Because of the complex of exchange regulations, and the possible effects of the Rome Treaty upon them, there appear to be important potential advantages in establishing an operating company in one of the Common Market countries, capitalizing it sufficiently so that it can engage in branch or subsidiary operations in other Common Market countries, and permitting earnings to accumulate to the extent that they may later be wanted for reinvestment in the other countries. It may prove a good deal easier to reinvest such earnings than earnings which have been remitted to the American parent

320 Id. art. 70(2), par. 2.
321 Id. art. 67(1).
or to a Swiss holding company. There is the incidental advantage that such earnings will escape the corporate income which they might incur if remitted to the American parent.

3. FLUCTUATING EXCHANGE RATES

Assuming that permits to invest can be obtained, the investor confronts the problem of minimizing (or maximizing) the risk of currency fluctuation. If lire have been bought with dollars, and the lire decline in exchange value, obviously the same number of lire will not repurchase the same number of dollars. Conceivably, the lire decline will be accompanied by an increase in nominal lire profits, so that more lire will be earned, and the same number of dollars can be repurchased. But there is no certainty that this will happen.

Considerations of this order apply differently to equity and to debt investments. To a foreign subsidiary, a dollar debt will be a dangerous thing, if the subsidiary is in a country whose currency is likely to fall more than the dollar; in terms of the local currency, it is a debt that grows. A dollar equity is quite different; since no fixed obligation is incurred, it does not matter so much if the dollar dividends shrink.

Considering these factors, American parent companies will not ordinarily want their European subsidiaries to borrow dollars, nor will the parent companies want to borrow dollars, to invest in the subsidiaries. They will want to invest equity capital from America, and to borrow money, if at all, in the country where the business is to be operated. If the rates of interest in that country are too high to permit advantageous “trading on the equity,” the correct conclusion will be to refrain from borrowing; it will not usually be wise to borrow money in another country (such as the United States or Switzerland) where interest rates may be lower, because such countries are likely to have currencies which will become dear in terms of the country where the interest must be earned.

One may be tempted to offset the potential loss from a foreign currency decline against the potential gain from a decline in American currency. An investor in Germany might contemplate the possibility that the German mark will be revalued against the dollar, and that his dollar debts will grow lighter, like a load of salt in a rainstorm. This is a dubious offset. In equity investments, the possibilities of loss may be offset against the possibilities of gain; but in fixed obligations, the possibility of loss is the possibility of disaster.
From these considerations, it follows that American investors will often be very much interested in the European market for loans, even though they are not interested in the European market for equity investment. This will probably be true even though all the European currencies now appear to be fairly stable; investment plans must contemplate the possible developments of future decades.

B. Equity Financing

I. Divided Ownership

Most American companies, we have found, have little interest in sharing their equity interests in foreign subsidiaries with other persons. We think the reasons are generally well-founded, and will become progressively more apparent during the transitional period of the Common Market. Any company which has a French subsidiary and a German subsidiary, each making pins and needles, will find increasing occasion to concentrate the pin-making activity in one, and the needle-making activity in the other; or to close both and build a new plant in Luxembourg. Decisions of this sort which are very clear from the viewpoint of the parent company may be directly against the interest of any one of the subsidiaries. If so, these decisions will also be against the interest of the minority holders in the subsidiaries. The parent must then make the unpleasant choice between losing operating economies, and losing the confidence of a group of local investors. Foreseeing this problem, it will probably prefer to retain all the shares except the few that must be held by others in order to maintain the minimum number of shareholders required by European company laws.

There are very few legal impediments to 99% ownership of a European affiliated company. Our French collaborator advises that France has laws requiring majority or complete ownership by nationals in French companies which operate a travel agency, an accounting business, or a bank, or which claim compensation for war damage. There may be other categories, but they are exceptional rather than typical.

The effect of these restrictions on Americans will be limited by the new U.S.–French Convention on Establishment, which permits exclusion of American interests only in “communications, air or water transport, banking . . . , exploitation of the soil or other

322 But cf. Ripert, op. cit., 454, stating that the law regarding travel agencies is the only one which makes an issue of the source of capital.
natural resources, and the production of electricity." 323 This treaty will forbid any direct prohibition on ownership, although it will not necessarily prevent the French from refusing to license currency exchanges for the purpose of buying interests in particular kinds of business. 324

A more important undermining of these restrictions arises from the Treaty. Under Article 221, each Common Market Country must permit investment by nationals of other countries to the same extent as investment by its own nationals. Under this clause, an American-owned Dutch subsidiary may own stock in a French company, even though the American company is forbidden to own directly. The sweeping terms of the directive of May 11, 1960, 325 indicate that exchange control will not be used as a means of blocking Dutch company investment in France.

Consequently, a 99% ownership of a European subsidiary seems to be legally attainable. However, there may be practical difficulties. If the American investor finds the right enterprise, its owners are not likely to be eager to sell out. If the American investor attempts to build a new enterprise, he must find a site, build a plant, buy equipment, hire labor and executives, and organize a distribution system, in a country where sites are generally more scarce, labor less mobile, trained executives less numerous, and distribution systems more tied up than in the United States—and in a country where he has to speak through interpreters.

American investors frequently decide that the perils of building a new enterprise are less than those of divided ownership. If they are able to find a European going concern which has plant and personnel and outlets, and which is willing to sell a substantial

324 Even if 99% ownership is permitted by law, it may be a factor which makes exchange control officials reluctant to grant investment licenses, as M. Jeantet suggests in his essay on exchange control. We have no similar reports from other countries of the Market. With respect to joint investment, a distinction may generally be drawn between European countries, which are themselves exporters of capital, and the "under-developed countries" of other continents, where there is a heightened sensitivity to foreign domination of ownership. The reasons which may dictate joint investment in those countries do not apply significantly to the member states of the European Economic Community. We have been privileged to see pre-publication manuscripts of an extraordinary series of studies directed by Professor Wolfgang Friedman of Columbia University on Joint International Business Ventures, which concerns joint investment in various countries by the United States and local interests. Among the countries discussed as investment locations are Burma, Cuba, India, Pakistan, Philippine Islands, and Turkey. There is a volume on Japan, but it concerns foreign investment by Japan in other countries.
portion, but not all, of its shares, many American investors will quite properly be attracted by this alternative. In the course of time, they will probably be trying to buy out the local interests, but this does not prove they did not make the best choice in joining with local interests rather than starting from scratch.

Which choice is to be preferred obviously depends on the characteristics of the particular choices that are available. We think it is safe to say that the building of a foreign business from scratch is for those American investors who have extensive prior foreign experience, who already have significant commercial contracts in the country where the enterprise is to be created, and which need facilities that are considerably different from any already available in the country in question. Investors without these advantages should generally seek to acquire existing enterprises, and settle for divided ownership if they cannot obtain 99%.

2. CONTROL DEVICES

In many cases, the American investor will want to know whether he can reserve voting powers which are proportionately greater than his equity investment. The first answer is that one cannot do it by any method so simple as the issue of non-voting common stock. The general rule in all six countries is that all shares vote.\(^{326}\) There are statutory exceptions in two countries—Germany and Italy—for preferred stock;\(^ {327}\) but preferred stock is no more fashionable in today's German and Italian capital markets than it is in America. Another familiar American device that is not likely to work in Europe is to have two classes of shares—one worth a dollar, and the other worth a hundred dollars—which have equal votes per share. Italy and Luxembourg require that all shares in stock companies have equal value.\(^ {328}\) Belgian, French and Dutch laws expressly provide that shares shall vote in proportion to the capital which they

\(^{326}\) Belgium: C. Com. I, IX, art. 74, as amended by Arrêté Royal No. 26 of Oct. 31, 1934, art. 3 (stock companies); C. Com. I, IX, art. 135 (limited liability companies).
France: Law of Nov. 13, 1933, art. 1 (stock companies); Law of March 7, 1925, art. 28.
Germany: AktG § 114 (1); GmbHG § 47.
Italy: C. Civ. 2351 (stock companies), 2485 (limited liability companies).
Luxembourg: Company Law arts. 71 (2) (stock companies), 195 (limited liability companies).
Netherlands: C. Com. art. 44b.

\(^{327}\) Germany: AktG § 115 (1); the shares must be cumulative without limit; and cannot exceed half of the voting shares.
Italy: C. Civ. art. 2351; the non-voting shares must not be more than half of all shares.

\(^{328}\) Italy: C. Civ. art. 2348.
Luxembourg: Company Law art. 37.
represent; 329 in other countries which have no similar statutes, this stratagem would probably be regarded as a violation of the general rule that all shares vote.

So far as European laws permit departure from the principle of voting in proportion to investment, the departure tends to dissipate control, rather than to concentrate it. Belgium furnishes an extreme example, with her law that a majority owner can never cast a majority of votes; a single voter cannot vote more than one-fifth of the shares outstanding, nor cast more than two-fifths of the votes cast at any meeting. 330 This is a rule of public policy, not alterable by the charter. Owning fifty-one percent of the stock is therefore no guarantee of control, unless the fifty-one percent is distributed among three different shareholders, who vote in harmony. Happily, this provision is not mandatory in other countries; the German law mentions it, but only as a permissible clause in the charter. 331

At the same time, France and Belgium offer a very interesting institution for recognizing investment without a grant of proportionate voting power. American lawyers will recall the problems which arose in the days of high-par stock with regard to mines or patents or good will exchanged for stock; if later events showed the property to be worth less than the par value of the stock, the contributors were in danger of liability. 332 This problem was solved in France and Belgium by invention of "founders'" and "beneficial" shares; 333 they are also known in Italy. 334 These do not purport to be contributions to capital, and do not share in capital distribution on liquidation; hence the specific value of the property contributed becomes immaterial. But these shares do receive dividends, just like other shares.

We have mentioned them at this point, because they do not neces-

329 Belgium: C. COM. I, IX, art. 74, as amended by Law of Nov. 10, 1953, art. 1, § 4.
France: Law of Nov. 13, 1933, art. 1.
Netherlands: C. COM. art. 44b.
330 C. COM. I, IX, art. 76.
331 AktG art. 114 (1). See also Neth. C. COM. art. 44b.
333 See HAMEL, TRAITÉ DE DROIT COMMERCIAL No. 566-68 (1954).
For statutory recognition of these types of shares, see:
Belgium: C. COM. I, IX, art. 75.
Law of Nov. 13, 1933, art. 1.
334 Beneficial shares (azioni di godimento) are mentioned by the statute only in connection with reductions of capital (C. CIV. 2353), but are believed to be usable in a variety of other circumstances.
sarily have voting rights. In Belgium, they may be given votes, but the total votes ascribed to such shares must not exceed half the votes ascribed to regular ("capital") shares; in counting votes, theirs must not be counted for more than two-thirds of the total counted for regular shares. 335

These special shares can be used in various ways to adjust voting power in a jointly-owned enterprise. If voting power is to be divided in a different ratio from profits, most of the shares (e.g., 9990) may be "beneficial shares," in the ratio desired for profit division, with a very small number of ordinary shares (e.g., 10) divided in the ratio desired for control.

There remain two more vote-shifting devices in French law which hold some interest for an American investor. One is the permission to create shares which have a double vote, when they have been held in registered (not bearer) form for two years. 336 Although this device was probably originated as a means of keeping American speculators from gaining control of French enterprises at times of currency devaluation, 337 and the charter may exclude foreigners from acquiring the double vote, 338 there is nothing now to prevent its being used to protect an American plurality. Another device is to exclude from attendance at meetings holders of less than a given number of shares, which may be set as high as 20, or one-twenty-thousandth (.0005) of the total capital (whichever is higher). 339 We mention these without any recommendation as to when they might be used, because we suspect that under most circumstances they would do more harm than good.

Various other devices employed in the United States to stabilize management in the presence of divided ownership are unavailable in the Community countries, and the voting trust (like other varieties of trust) is unknown, except in the Netherlands.

Voting agreements between different groups of security holders are evidently in use, but their enforceability is dubious at best. In France, any agreement which limits the voting freedom of a stock company shareholder is declared to be invalid. 340 However, the law is not thought to forbid caucuses in which groups of shareholders agree as to how they will vote, without actually binding themselves;

335 C. Com. I, IX, art. 75.
336 Law of Nov. 13, 1933, art. 1.
337 See HAMEL, TRAITE DE DROIT COMMERCIAL No. 547 (1954).
338 Law of Nov. 13, 1933, art. 1.
339 Ibid.
340 Law of Nov. 13, 1933, art. 4, as amended by Decree-Law August 31, 1937.
nor does it apply to agreements among governing board members. The law does not purport to apply to limited liability companies; voting agreements as to them are presumably valid, and may be further cemented by the previously mentioned restrictions on share transfers,341 and appointment of a manager for an indefinite or a long term who cannot be removed without cause.342

In Germany, there is no law against voting agreements, but there is a criminal law against giving a consideration for a stock company shareholder’s vote.343 Presumably this does not forbid an exchange of voting promises among shareholders, but penalizes the taking of some extraneous monetary consideration.

In Belgium, a leading commentator believes that all voting agreements are invalid.344 An earlier Italian view to the same effect has recently given way to the view that agreements among shareholders as to how they will vote their own stock are legal; but they will not be specifically enforced, and a shareholder cannot separate himself from the voting power.

Possibilities of proxy control may also be considered. In France and Germany it appears that proxies can never be irrevocable;345 a Belgian commentator believes they can be irrevocable there, within reasonable limits.346 There are no such rules about proxy solicitation as we have in the United States under section 14 of the Securities Exchange Act, but the Netherlands forbid solicitation by members of the governing board.347 In other countries, management solicitation of proxies is apparently untrammeled, and “proxy control” exists in many large European companies. But this would seem to be of little interest to American investors in subsidiaries or affiliates, since the shareholders are unlikely to be so dispersed as to make proxy control effective.

Only in the Netherlands do we find clear judicial approval of voting agreements among public shareholders,348 and common usage of a well-recognized medium for company control by agreement of the investors—the voting trust. This operates much like an Ameri-

341 Law of March 7, 1925, art. 22.
342 Id. art. 24.
343 AktG § 299.
344 Van Ryn, 1 Prin. de Droit Commercial No. 707 (1954).
345 France: Hamel, op. cit. supra note 337, No. 533.
346 German: AktG § 114(4).
347 W.K. art. 44a.
348 Hooge Raad, June 30, 1944, Nederlandsche Jurisprudentie 1944, No. 465.
can voting trust. It is of considerable interest to American participants in a "joint investment" with Dutch investors; they might agree on a board of voting trustees which contained representatives of each investing group, plus some neutral party chosen from a Dutch bank (for instance), or even from another country.

3. KINDS OF SHARES: DEGREES OF NEGOTIABILITY

In the matter of shares, European companies have a variety of forms which have no parallel in America. Our kind of shares—registered in the name of the owner, but negotiable by indorsement and delivery—does not exist in Europe. Instead, they have three other kinds of shares, one of which is found in limited liability companies, and the other two in stock companies.

For simplicity, we will start with the limited liability company share (called part, Anteil, parte, and deelbewijs, in the various languages). It is more like a share in an American partnership than like a share in an American corporation. It is never negotiable, never eligible for public issue, never listed on stock exchanges, and frequently transferable only with consent of the company or the other shareholders. It resembles a share in an American corporation only in that it is a unit of stated value, identical with others in the same company.

In stock companies, the share is so differently conceived by Europeans that they give it a different name from the limited liability company share. It is an action, Aktie, azione, or aandeel, and it is so distinctive that in Germany and Italy this kind of company is named for the kind of shares it issues—Aktiengesellschaft or società per azioni. The outstanding feature about the stock company share is the fact that it can be put in a negotiable form, which can be transferred endlessly from owner to owner.

[349] Not all these negative characteristics are explicitly stated in the limited liability statutes; more often they are implied from the fact that the statute used the word which applies to partnership shares, rather than the word which applies to stock company shares, and fails to authorize negotiable features. See the following:

Belgium: C. Com. I, IX, art. 124–25 (shares not transferable even between parties without entry on company books).

France: Law of March 7, 1925, art. 22–23 (shares not transferable without consent of fellow-shareholders; transfer ineffective for any purpose until registered).

Germany: GmbHG § 15 (share transfers must be notarized).

Italy: C. Civ. art. 2479 (no special provisions, but no such authorization for bearer certificates as is made for stock companies).

Luxembourg: Company Law, art. 189 (no transfer without consent of other shareholders).
with no registration, just like money; this form is the "bearer share" (action au porteur, Inhaberaktie, azione al portatore, aandeel aan tonder).\textsuperscript{350}

The bearer share is the typical share in publicly held European stock companies, with many interesting consequences. One of these is that when war breaks out, shareholders who are nationals of an enemy country, but whose identity is unknown, may be able to sell their holdings in Switzerland, rather than having them seized as enemy property at the home of the company. Another consequence is that the principal holders of shares in large companies may readily remain unknown, so that questions of "control" which have become prominent in proceedings of the American Securities Exchange Commission, Interstate Commerce Commission, or Anti-Trust Division can hardly be even discussed in Europe. Likewise, there is unlikely to be any knowledge of the "insider trading" which has given rise in this country to statutory liabilities under Securities Exchange Act section 16(b) or Securities Exchange Commission Rule X-10-b-5.

The absence of a record of ownership has necessarily led to other practices which are unknown in the United States. Share certificates have attached to them coupons which are deposited in banks for collection of dividends, like American interest coupons, even though the amount of the dividend varies each year, or may be nothing. The company has no idea as to who is the recipient of the dividend, and cannot report him to the income tax collector. In order to establish the right to vote, certificates may be deposited with a bank, which certifies as to the number deposited, and generally exercises the owner's proxy.\textsuperscript{351} If the owner does not give directions, the banker exercises his own judgment. In this way, shareholder apathy in Europe gives great power to bankers instead of, as in the United States, to company management.

The other kind of share in a stock company we will call by the familiar American name of "registered share," although some writers prefer to call it "nominative share" (action nominative,

\textsuperscript{350} Belgium: C. Com. I, IX, art. 45.
France: C. Com. art. 35.
Germany: AktG § 10.
Italy: C. Civ. art. 2355.
Luxembourg: Company Law art. 37.
Netherlands: W.K. art. 38c, 38d.

\textsuperscript{351} The proxy-holder must disclose that he votes as agent, in Belgium and Luxembourg. It is forbidden to vote "as owner" shares belonging to another. Belg. C. Com. I, IX, art. 200; Lux. Company Law art. 162.
Namensaktie, azione nominativa, aandeel op naam). Although bearer shares are generally preferred by European investors, registered shares play a considerable role.

In Italy, there are currently no bearer shares. Measures of economic warfare, adopted almost twenty years ago, required that all shares be put in registered form.\textsuperscript{352} These have been kept in effect, presumably for the aid which they give to enforcement of taxes, exchange control, and other legislation.

In other countries, too, shares are sometimes required to be registered for financial reasons. Everywhere, shares must be registered until their full value has been paid in to the company.\textsuperscript{353} Under the codes of French inspiration, shares which are issued in exchange for property are required to be registered for a "cooling off period,"\textsuperscript{354} or else (in Luxembourg) deposited in the company treasury.\textsuperscript{355} The objective is to delay speculative trading until the securities are adequately "seasoned." Where governing board members are required to be shareholders, the required shares must be registered in their names.\textsuperscript{356}

How great a disadvantage it is to have a share in registered, instead of bearer form, we have not been able to tell. It seems clear that outside of Italy, shares must be in bearer form in order to be acceptable to buyers on organized security markets. But in Italy, share trading seems to have revived on and off the exchanges without the aid of bearer shares. Since the registered share has not long been an article of commerce, we suspect that the European law is

\textsuperscript{352} Decree-Laws of Oct. 25, 1941, No. 1148; March 29, 1942, No. 239.
\textsuperscript{353} Belgium: C. Com. I, IX, art. 46.
Germany: AktG § 10(2).
Italy: C. Civ. art. 2355.
Luxembourg: Company Law, art. 43.
Netherlands: W.K. art. 38c.
\textsuperscript{354} Belgium: C. Com. I, IX, art. 47 (until ten days after the company's second annual report is published).
France: Law of 1867, art. 3, as amended by Decree of Dec. 7, 1954 (shares "not negotiable" and certificates not to be issued until two years after incorporation).
Italy: Cf. C. Civ. art. 2343 (shares issued for property not transferable at all until property is appraised by an expert, and appraisal reviewed by board members and auditors).
Luxembourg: Company Law art. 44 (shares not negotiable until 10 days after the second annual report of the company is published) 47.
\textsuperscript{355} Company Law art. 47 § 2.
\textsuperscript{356} Belgium: C. Com. I, IX, art. 57.
France: Law of 1867, art. 26 (further, certificates must be deposited in company treasury, and stamped to show that they are not transferable).
Luxembourg: Company Law art. 54.
I 3 2 AMERICAN ENTERPRISE IN THE COMMON MARKET

much like that of the United States before adoption of the Uniform Stock Transfer Act; that is, somewhat unsettled, but not wholly incompatible with reasonable stock trading.

4. FORMALITIES REQUIRED TO INCREASE CAPITAL.

We have mentioned before that the capital stated in the articles of association must have been 100% subscribed at that time. And unless it has all been paid in, no more may be offered. Consequently, the governing board cannot casually sell some additional shares when the market seems favorable, and when the company needs the money.

In most kinds of companies, any addition to equity capital must start with an amendment of the charter, accomplished by a statutory majority of the shareholders. The increased capital must also be 100% subscribed before the increase is fully effective. There may be further requirements to ensure that all the subscriptions are fully paid.\textsuperscript{357} The principal exception is the Netherlands, in which the liberty of forming a company with only one-fifth of its capital subscribed applies also to capital increases.\textsuperscript{358}

Two countries—France and Germany—permit the original charter to contain authorization for the capital increase. In France, a company with this power is called a stock company “with variable capital,” (société anonyme à capital variable) and must so describe itself. It can revise its capital downward as well as upward.\textsuperscript{359} In Germany, there is an arrangement known as “authorized capital” (genehmigtes Kapital),\textsuperscript{360} but it works quite differently from “authorized capital” in the United States.\textsuperscript{361} When the decision to increase is made, the increased capital must be 100% subscribed and 20% paid in, just like the original capital. The only advantage over an amendment to increase capital is that the decision may be made by the executive board, rather than by the shareholders.

The necessity for 100% subscription of the capital which a company has power to issue is a very real one. If less than 100% is

\textsuperscript{357} All the limited liability laws, and some of the stock company laws are silent on increase of capital; in these circumstances, lawyers apply by analogy the provisions for original issue of capital, which have been described earlier in connection with corporate formation. Specific provisions on increasing the capital appear in Germany: AktG art. 149-158. Cf. Neth. C. Com. art. 45d, para. 2.

\textsuperscript{358} W.K. art. 366; 45d, para. 2.

\textsuperscript{359} Law of 1867, art. 48-54. Most lawyers see no practical advantage in the use of these provisions; they prefer to form a company with fixed capital, and amend later. AktG § 169-173.

\textsuperscript{360} See Pueck, Gesellschaftsrecht 170-171 (2nd. ed. 1948).
subscribed, the increase is not effective; those who have subscribed are not bound to pay (unless the capital is formally reduced), and the board members are forbidden to issue shares to them. 362

Naturally, European businessmen have learned to avoid any such fiasco. The simplest way is to canvass the prospective subscribers before the capital increase is authorized, so that the amount authorized may coincide with that which they will actually subscribe. This method is practical only where the new shares are to be issued to a small, known group.

A second way to escape the rigidity of the 100% subscription requirement is to put a clause in each subscription agreement that the amount of the total capital increase may be reduced without effect on the subscription. Then, when the subscriptions are all in, and their amount known, the shareholders may amend their former amendment, to adjust the capital increase to the subscriptions obtainable. 363 This method is cumbrous, and may tend to cloud the atmosphere of confidence in which share subscriptions are best solicited.

A third method is to obtain 100% subscription in advance from investment bankers, who thus underwrite the risk that the investment public will not take the entire issue at the price proposed. 364 This is the standard device used in large public financing operations. The importance of having a firm bid seems to be considerably greater than in the United States.

Although the underwriter must promise the issuer to take the entire issue, the issuer can never promise the underwriter that he will get it. The first opportunity to take the new shares generally belongs to the old shareholders. The company laws confer unconditional pre-emptive rights only in France and Germany, 365 but these rights appear to exist in all countries, at least unless specifically negatived, as permitted by Italian law. 366 Pre-emptive rights adhere to preferred shares as well as to common—a factor which aggravates companies' reluctance to issue preferred shares. Because of

362 France: Law of 1867, art. 7, 42.
Germany: AktG § 152, 84 (executive board members liable); cf. AktG § 158.
363 Belgium: VAN RYN, DROIT COMMERCIAL no. 489 (1954); Frédéricq, 4 DROIT COMMERCIAL 494–95 (1950), quoting parliamentary debates of 1870.
364 Escarra, supra note 363.
Germany: AktG § 153.
366 C. Civ. 2441.
the European recognition of indefeasible pre-emptive rights, underwriting arrangements generally have a contingent element; what the underwriter agrees to take is what the shareholders reject.\textsuperscript{367}

C. FINANCING WITH BORROWED FUNDS

Most American investors will be much more interested in obtaining outside financing in the form of borrowed funds than in the form of stock subscriptions. Aside from the problems of divided ownership, there is the important fact that debt interest is generally deductible from taxable income (just as in the United States), while dividends on stock (even preferred stock) never are. We have been warned of only a few exceptions to the deductibility rule. In France, interest is not deductible when paid to shareholders under circumstances that lend themselves to disguised equity investments;\textsuperscript{368} in the Netherlands, contingent interest is sometimes non-deductible.\textsuperscript{369}

I. TRADING ON THE EQUITY;
OBSTACLES TO THE USE OF "LEVERAGE"

Some other classical advantages of borrowing money—summed up in the phrase, "trading on the equity,"—are probably also present in Europe, but with qualifications which must not be ignored. One of the presuppositions of "trading on the equity" is that interest rates are lower than dividend rates. Here we must notice that the same kind of inversion recently observed in the United States may exist in Europe. That is, the interest rate may become higher (or at least as high as) the dividend rate. In 1959, the German Central Bank Discount rate fluctuated between 2-3/4\% and 3\%, which would mean a rate of at least a percent higher to commercial borrowers. In August, the average yield on stocks listed on German stock exchanges was 2-3/4\%.\textsuperscript{370} Hence, the cost of equity capital was apparently lower than the cost of borrowed capital.

Perhaps the modern theory of "trading on the equity" rests not so much on a difference in contemporaneous income rates, as upon

\textsuperscript{367} For an interesting account of an international underwriting of a European share offering, see Bross and Alpern, International Equity Financing, 13 BUS. LAW. 440 (April 1958).

\textsuperscript{368} Professor Houin advises that deductibility is denied as to interest paid on debts owed to shareholders when (1) the interest exceeds a certain rate, or (2) the debts so owed amount to more than half the equity capital.

\textsuperscript{369} In cases of "participating" bonds, whose "interest" rate rises in proportion to company profits, the tax collector asserts a right to regard part of the participation as a distribution of profit, rather than a payment of interest.

a supposition that dividend rates will rise (in relation to the initial investment), while interest rates will not. This supposition would also be belied by important features of the European financial scene. The most important of these is the decline of fixed interest obligations, and their partial replacement by obligations which "inflate."

The inflatable securities are of three types. One type is the bond convertible into stock; it is essentially like the well known convertible debenture of American finance (although the problem of providing the shares for conversion presents special legal difficulties because of the European limitations on "authorized stock").

A second type is the "participating" bond, on which the interest to be paid varies with the income of the company. It should not be regarded as equivalent to the "contingent interest" bonds which were issued chiefly in reorganizations of insolvent American companies, and which had a fairly low top limit on the maximum interest to be paid (for instance, 2% fixed and 3% contingent). The European variable interest bond generally permits an unlimited increase in the income rate as the company income rises, the objective being to let the purchasing power of the interest escape from the deadly embrace of the sinking franc (or other currency).

A third type of inflatable bond—and the most unlike any investment familiar to Americans—is the "indexed" bond, in which the interest to be paid, and the principal to be repaid, rise in proportion to increases in some official index, such as the index of wholesale prices, or the cost-of-living index.

Obviously, all these forms of debt security diminish greatly the possibility of "trading on the equity." The convertible bond tends to limit the leverage to the time before conversion, after which the advantage disappears. The "variable interest" bond tends to take away all leverage. The indexed bond may even have a reverse leverage, if the company's profits have the misfortune to rise less than the increase in the relevant price index.

Naturally, the flight from fixed interest has been most marked in the countries where currency devaluation has been felt most sharply. In 1954, French nationalized industries borrowed 3 billions on fixed income securities, against 67 billion on participating or indexed securities, according to a study of European finance. Private industries borrowed, respectively, 9 billions and 35 billions in the

---

372 Alamigeon treats this as one kind of "indexed" bond. Id. 64-65.
373 Id. 63-64.
same categories, respectively.\textsuperscript{374} Writing in January of 1959, our French collaborator declares, "For practical purposes, the only debt securities presently being issued by companies in France are either securities with variable interest, or convertible securities; fixed interest securities of the classic type are becoming more and more scarce." He reports that in 1957, only one billion out of 59 billions of bonds were of non-inflatable types.

However, there has been a change in the choice of inflatable media. While the earlier reports emphasized the use of what we call "indexed" bonds, the most recent issues are of the "participating" type. A financial regulation issued at the close of 1958 (contemporaneously with the relaxation of currency controls) forbade the issue of bonds indexed to the minimum wage or cost of living, but imposed no obstacles to bonds whose interest varies with the fortunes of the enterprise, as measured by revenues or profits.\textsuperscript{375}

Apparently there has been no comparable development in other European countries. In Italy, which has also experienced severe currency depreciation, there has been little use of inflatable debt securities. Equity financing has displaced debt financing to a marked extent; in 1955, the ratio of private share issues to private bond issues was 162 to 9; and it had been growing steadily.\textsuperscript{376}

The O.E.E.C. report on Germany also pointed to a tremendous predominance of equity issues over debt issues (156 to 9 in 1955);\textsuperscript{377} convertible offerings disappeared after a brief flurry in 1951 and 1952.\textsuperscript{378} In the Belgium-Luxembourg Monetary Union, which has had the stablest of the European currencies since 1945, there have been no notable developments of any of the three types of inflatable debt securities.\textsuperscript{379}

2. LIMITS ON DEBT OBLIGATIONS

As in America, the principal forms of debt obligations are (1) bonds, designed for sale to a variety of investors, and (2) bank

\textsuperscript{374} O.E.E.C., \textit{The Supply of Capital Funds for Industrial Development in Europe} 80 (1957). This report appears to use "indexed" to include interest varying with factors extraneous to the enterprise (like the cost of living), and "participating" to designate interest varying with the gross revenues, operating income, or net profit of the enterprise.


\textsuperscript{376} Ordinance of Dec. 30, 1958, portant loi de finances pour 1959, art. 79.
\textsuperscript{377} O.E.E.C., \textit{op. cit.} 97.
\textsuperscript{378} Id. 82.
\textsuperscript{379} Id. 83.
loans, which may be discounted among banks, but which are not available to a broad investing public.

However, many companies are incapable of issuing bonds. This is true of limited liability companies in Belgium, France, Italy and Luxembourg.\textsuperscript{380} This limitation is apparently based on the belief that the streamlined organization of limited liability companies deprives the investor of the protection which he has in buying the bond of a stock company. When limited liability companies borrow money, they must borrow it from banks, which are professional lenders; the rule against issuing bonds is not construed to forbid giving notes to banks. This does not mean that limited liability companies have access only to short term credit; bank loans in Europe include "medium term" and even "long term" credits.

Another distinctive limit on the use of bonds is the Italian provision which, with certain exceptions, limits the bonds which a stock company may issue to the amount of its capital stock.\textsuperscript{381}

3. SOURCES OF CREDIT

Observers of European finance over the past fifteen years stress the scarcity of investment funds during most of this period in relation to the exaggerated demands of post-war reconstruction. In addition to these factors, which operated equally on equity capital and borrowed capital, there was a special aversion to lending, inspired by the experience of inflation and the expectation of more of the same.\textsuperscript{382}

Because of these factors, the European governments were obliged to create or encourage new institutions with the specific function of supplying credit to industry on a longer term than commercial banks were prepared to do.\textsuperscript{383} Most of this credit is what is called "intermediate term," ranging from one to five years, but often with an expectation of renewal so that it fulfills the economic function of true long-term credit.

In France, the outstanding institution of this type is the Crédit


\textsuperscript{381} C. Civ. art. 2410.

\textsuperscript{382} See O.E.E.C., THE SUPPLY OF CAPITAL FUNDS FOR INDUSTRIAL DEVELOPMENT IN EUROPE (1957), and Supplements I and II, containing detailed studies of Finance in Austria, Germany, United States, Belgium, France, Greece, and Italy; VASSEUR, DROIT DE LA RÉFORME DES STRUCTURES INDUSTRIELLES (1959) 178 ff.

\textsuperscript{383} See O.E.E.C., op. cit. note 382, at 45 ff.
It acts by discounting notes taken by commercial banks, and rediscounting them to the Bank of France or another central bank. The net cost of the loan is based on the Bank of France discount rate plus the discounts and commissions of intervening agencies. A 1958 report indicated that the rate to a borrower would be 7.6% at a time when the Bank of France discount rate was 5%; the latter rate was reported in 1959 as low as 4 1/4%.  

In addition to the Crédit National, which extends intermediate credit, France has the Crédit Foncier, which extends long term credit secured by real estate, and some smaller semi-public credit institutions with various specialities. These institutions, including the Crédit National, are tremendously important; they are the principal source of fixed-interest credit. In a year in which private and nationalized companies succeeded in borrowing only 12 billions from the public in fixed-interest obligation, the Crédit National rediscouted 46 billions in fixed-interest notes. In the same year 64 billions were raised by private and nationalized industrial companies by participating or indexed bonds. The activities of the Crédit National may decline if the recent stabilization of the French economy results in a revival of private lending at fixed interest. But at our last reports, private industry's needs for finance depended very heavily on the Crédit National.

Semi-public and public lending institutions play a prominent role also in most of the other countries of the Market, although statistics on their activities are not equally available. In Italy, the most important three are the Istituto Mobiliare Italiano (I.M.I.), which makes direct loans to industry, and the Mediocredito which discounts industrial loans made by private banks. Both are owned by the state. In Germany, there is the state-owned Kreditanstalt für Wiederaufbau (KfW) which had outstanding loans or loan commitments of 5,790 DM in 1954, compared with 741 DM loans by the largest private long-term lender, the Industriekreditbank (I.K.B.).

In Belgium, the principal resource available for intermediate

---

385 Alamigeon, op. cit. note 372, at 120.
388 O.E.E.C., op. cit. note 383 at 54, 80.
389 Id. 59–62.
390 Id. 51–54.
and long-term credit since 1946 has been the semi-public loan companies, of which only one—the Société Nationale de Crédit à l'Industrie—makes loans to industry. Not only has it been the principal source of such funds, but it also offers subsidized interest rates as low as 2% for the development of facilities designed to relieve unemployment in depressed areas. Private banks also extended intermediate credit, but under substantial handicaps. An avenue for increased industrial financing by private banks was opened by measures taken in 1959, permitting private banks to make long term loans, subsidized or guaranteed by the government.

So far as we can determine, the facilities of these public and semi-public lending institutions are just as available to American-owned enterprises as they are to locally owned ones; we know of some American-owned enterprises who have had no difficulty in using their facilities. If their attitudes differ from those of purely private lenders, it is chiefly in insisting that the borrowing enterprise should be of apparent benefit to the national economy. Although there may be a gradual expansion of the market for private financing in the coming years, we believe that many American owned enterprises will continue to find their cheapest and most satisfactory source of financing in government-owned credit institutions.

4. INTERNATIONAL CREDIT SOURCES

We have spoken of credit entirely in national terms—French credit institutions for France, Italian credit institutions for Italy. Such is certainly the existing pattern of European credit; the reasons are many and obvious. For one thing, most of the credit is not spontaneous profit-seeking activity, but is supplied directly or indirectly by the government to help the industry in the country whose government supplies the credit. The hazards of fluctuating currencies have offered a further obstacle to international credit.

But it is obvious that if there is to be a truly European development of industry and commerce, there must be a truly European supply of credit. Two possible forerunners of a European credit supply are now visible on the horizon.

One of these is the European Investment Bank, provided for by

391 Id. 62–65.
392 Id. 35–36.
393 Byé, Localisation de l'Investissement et Communauté Economique Européenne, Revue Économique 1958, 188.
the Treaty of Rome. Its members, and the contributors of its capital, are to be the six countries of the Community. Its purposes are stated as follows:

The task of the European Investment Bank shall be to contribute, by calling on the capital markets and its own resources, to the balanced and smooth development of the Common Market in the interest of the Community. For this purpose, the Bank shall by granting loans and guarantees on a non-profit-making basis facilitate the financing of the following projects in all sectors of the economy:

(a) projects for developing less developed regions;
(b) projects for modernising or converting enterprises or for creating new activities which are called for by the progressive establishment of the Common Market where such projects by their size or nature cannot be entirely financed by the various means available in each of the Member States; and
(c) projects of common interest to several Member States which by their size or nature cannot be entirely financed by the various means available in each of the Member States.\(^\text{394}\)

In its first two years of operation, the bank made seven loans, all of which had some special appeal to the interests of the Community. Six of these were in under-developed areas—two in southern Italy, two in southern France, one in Sicily, and one in Sardinia. The other was in Luxembourg. Four of the loans were for electric power generation, and three for chemical plants.\(^\text{395}\) An American company—Union Carbide—was an indirect beneficiary of one of the loans, through its part ownership in the new Italian company to which the loan was made.\(^\text{396}\) So far as conclusions can be drawn from so short a history, American investors are not barred from benefiting from European Investment Bank loans (at least, not when they are joint investors). But priorities will go to projects which promise to beget further productive products. The Bank's Board of Directors reports,

The projects to which the Bank has agreed so far, belong to the category of development investments intended for increasing basic productions which, in turn, contribute to increased demand, production, and invest-

\(^\text{394}\) Treaty art. 130.
\(^\text{396}\) Id. (1958) 20–22.
ment in many related fields. They are nearly all situated in the less developed areas of the Community, require fairly large amounts and are by their very nature, highly capital-intensive. 397

In the private banking sector, the commercial banks of the various countries have recognized the probable call for international loans. They are preparing for it to the extent of making contacts between banks, so that coordinated loans can be made in (for instance) francs and marks. 398 But there is no present prospect of a single private bank which will make a loan to a wholly out-of-state company, as is done every day in New York or Chicago. 399

D. Securities Regulation; Public Offerings of Securities

It is commonly said that European countries, except Belgium, have no securities or "blue sky" laws, and no securities commissions. This is true. But this does not mean that Europe is like America would be if all the securities and blue sky laws were repealed. European countries have a considerable number of laws and regulations which restrict security offerings, and which we will briefly explain.

397 Id. (1959) 14. For further comment on the possible role of the European Investment Bank, see Vasseur, op. cit. supra note 382, 351 ff.

398 Vasseur (op. cit. note 382, at 357) reports the following international organizations to promote international loans:

Société Européenne de Développement Industriel, a stock company formed by one French and one German bank (the Banque de Paris et des Pays-Bas, and the Deutsche Bank) to investigate and arrange cooperation between banks and other companies of the two countries.

Société Franco-Italienne de Développement Industriel, a stock company formed by one French bank and two Italian banks (the Banque de Paris et des Pays-Bas, the Banca Nazionale del Lavoro, and the Instituto Mobiliare Italiano) for parallel purposes.

Groupement Franco-Allemand pour le Marché Commun, an informal association of several French and German banks to consult on concurrent participation in loans to Common Market enterprises. The banks include (for France) Banque Française du Commerce Extérieur, Banque Louis-Dreyfus et Cie, Banque de l’Union Parisienne, Crédit Lyonnais, Société Générale, Société Générale Alsacienne de Banque, and (for Germany) Bankhaus Hardy and Co. GMBH, Bankhaus Sal. Oppenheim Jr. and Cie., Bayerische Hypotheken- und Wechselbank, Dresdner Bank AG.

Another informal association groups banks of five countries, comprising Berliner Handelsgesellschaft, Crédit Commercial de France, Compagnie Financière de Paris, Banque Lambert (Brussels), Banca di Credito Finanziario Mediobanca (Milan), Compagnie d’Outremer pour l’Industrie et la Finance (Brussels), Pierson Heldring et Pierson (Amsterdam), MM. de Rothschild Frères (Paris).

399 Vasseur (op. cit. note 382, at 357-358) prognosticates hopefully, but without detail, direct appeals by companies of one country to investors of another.
1. EXCLUSION OF LIMITED LIABILITY COMPANIES

The law about public offerings by limited liability companies is very simple. No public stock offerings of limited liability companies are permitted in any country, and no public bond offerings except in Germany.\textsuperscript{400} The theory of these laws is that the simplified structure permitted for limited liability companies—a single manager, with no watchdog auditors—affords so little investor protection that the solicitation of investment by strangers cannot be permitted.

2. REGISTRATION OF STOCK OFFERINGS

The absence of separate "securities laws" in most European countries is somewhat illusory because there are certain features built into the European stock company laws which contain the basic elements of American "securities registration," as well as features which may recall the reporting provisions of the Securities Exchange Act.\textsuperscript{401}

We will start with the German stock company law, which is the most elaborate. When new stock is offered, each buyer must write his signature on a declaration which discloses the number of shares of each class offered and their offering price, and names a date on which subscribers will be released if 100\% of the capital has not been subscribed.\textsuperscript{402} If shares are to be exchanged for property, the declaration must also show the name of the person making the exchange, the identity of the property, and the par value of the shares for which it is being exchanged.\textsuperscript{403} When all the stock has been subscribed, the company managers must file as a public record copies of

\textsuperscript{400} Belgium: As to shares, deduced from C. Com. I, IX, art. 119 (limiting number of shareholders to 50, and excluding corporations), 126 (restricting transfer) etc.; as to bonds, expressly stated by art. 131.

France: Law of March 7, 1925, art. 4 (forbidding public issue of securities of any kind).

Germany: GmbH § 3, 5 (requiring that entire capital be subscribed by incorporators).

Italy: As to shares, the result is deduced from C. Civ. art. 2472, which forbids issuing "azioni," meaning negotiable shares. As to bonds, C. Civ. 2486 forbids their issue.

Luxembourg: Company Law art. 188.

\textsuperscript{401} For some general comparisons of the regulation of security issue in United States and Europe, see Kessler, The American Securities Act and Its Foreign Counterparts, 44 Yale L. J. 1133 (1935); Levy, Private Corporations and Their Control 408-428 (1950); Neff, A Civil Law Answer to the Problems of Securities Regulations, 28 Va. L. Rev. 1025 (1942).

\textsuperscript{402} AktG § 152.

\textsuperscript{403} Id. arts. 152(1), 150.
the subscription certificates, of the contracts for issue of shares in exchange for property, a statement of the expenses of the flotation, and the governmental authorization (if required) for the offering. They must also publish a notice of the completed stock subscription, which includes a statement of the subscription price and of the property exchanged for shares (if any).

In France, capital increases are treated just like the original formation of the company. Subscribers must sign a subscription contract which discloses the name, purposes, and home office of the company, which shows how many shares will be paid for in cash and how many in property, and which tells where subscription payments are to be escrowed until the required sum is completed. If property is exchanged for shares, there must be an auditors' report and a meeting of shareholders to approve the exchange. The amendment which authorized the capital increase, and a certified copy of the subscribers' list, must be publicly filed, and a notice published in the Bulletin of Compulsory Legal Notices.

With variations in detail, there are similar provisions in the company law of Italy and Luxembourg to assure that the subscribers know what they are buying, and to make a public record of the fact of subscription.

Only in the Netherlands is the solicitation of subscriptions substantially unregulated by law, like intra-state solicitation in Delaware and New Jersey. But the absence of legislation is supplied, at least in part, by rules on registration of securities for trading on stock exchanges. These are rules imposed by the brokerage fraternity, which, like many other professional groups in the Netherlands, exercise substantial powers of economic control. The significance of stock exchange regulations is considerable; since there is no well-developed "over the counter" market outside the exchanges, the exchanges comprise the only market that exists.

3. LICENSING OF PUBLIC OFFERINGS

In spite of the absence of "Securities Commissions," it is necessary in every country but Luxembourg to obtain either the authori-

404 Id. art. 155.
405 Id. art. 157.
406 Law of 1867, as amended by Decree of Aug. 4, 1949, art. 28.
407 Law of 1867, art. 4.
408 Law of 1867, art. 55-57, 59.
409 Italy: C. Civ. art. 2333-2336.
Luxembourg: Company Law art. 33-36.
The principal difference between these systems and those of American security commissioners lies in the criteria of the authorization. In Europe, the main purpose is to prevent "disturbance of the market." Only in Belgium is the regulation of public issues avowedly designed partly to protect investors. The prevailing theory is that if too many securities were offered at a time, the market would be glutted, to the damage of all the concurrent offerors. European commentators emphasize the "thinness" of the European investment market—the limited amount of funds looking for placement. In most of the years since 1945, European markets have been "thin" as a result of the devastation of war, complicated by narrow national boundaries, which funds cannot pass without exchange permits. With financial recovery, and the recovery of vigor in European capital markets, licenses have become quite freely obtainable.

Consistent with the purpose of maintaining market equilibrium, licenses are not generally refused, but merely postponed. But they are not necessarily postponed in order of application. On the contrary, the finance ministries authorize offerings in their order of importance to the national economy. Under this test, government bond issues always come first; other issues must wait until government bond issues are fully subscribed. After that, priorities are granted on a wide variety of economic grounds; an offering which will tend to increase facilities of production for export is more desirable than one which will merely satisfy domestic consumer demands. An offering to finance a plant in a distressed area is more important than one for the same purpose in an area of labor scarcity. If there

410 Belgium: Arrêté Royal No. 185 of July 9, 1935, art. 26–34.
France: Law of Dec. 23, 1946, art. 82.
Italy: Law of May 3, 1955, No. 428 (offerings over 500 million lira—about $750,000).
Netherlands: No statute requires licensing, but (1) by a gentleman’s agreement brokers will not handle the shares unless the offering has been approved by the Nederlandse Bank, and (2) the Minister of Justice will withhold permission for any incorporation or charter amendment until he is satisfied with respect to the financing plans.

411 The Belgian law discloses two purposes; the offering can be postponed because of a tendency to "déséquilibrer le marché des capitaux" (art. 28) Arrêté Royal of July 9, 1935, or to "induire les souscripteurs en erreur." (art. 29), Arrêté Royal, No. 185 of July 9, 1935. The French law declares no purposes, but it is attached to a government budget bill, and is reportedly administered chiefly to protect the market for government bonds.

Under the German law, "Die Genehmigung kann versagt werden, wenn Zinssatz, Ausgabe- und Rückzahlungsbedingungen bei gleichartigen Wertpapieren wesentlich abweichen und bei einer Genehmigung eine nachhaltige Störung des Kurs- und Zinsgefüges am Kapitalmarkt zu befürchten wäre."
is a national plan of industrial development, as in France, conformity to the national plan will be important.

Another difference in result which flows from the difference in purpose is that when money is "easy," licenses are granted with great freedom, or a "general license" is granted, which means in effect a suspension of the regulation.\textsuperscript{412}

4. THE BELGIAN BANKING COMMISSION

Two years after the adoption of the federal Securities Act in the United States, Belgium created a "Banking Commission," with powers over the public issue of securities.\textsuperscript{413} Probably the primary object of the creation was the supervision of banks, and enforcement of the divorce, ordered by the same law, of investment functions from commercial banking functions.\textsuperscript{414} In any event, the Belgian Banking Commission, as its name suggests, supervises banking in general as well as securities issues.

The powers of the commission over securities issuance rest on the narrow basis of the power to postpone for a maximum of three months the issue of securities, and to publish its decision (with reasons).\textsuperscript{415} When one thinks of the great power wielded by the American Securities Exchange Commission through granting or withholding the acceleration (by a maximum of 20 days) of the effective date of registration statements,\textsuperscript{416} one can perhaps appreciate better the de facto influence of the Belgian commission.

The Commission's decision to prohibit (temporarily) may be based on either of two grounds—that the offering is likely to unsettle the capital market,\textsuperscript{417} or that it is likely to mislead investors as to the character of the business or the rights conferred by the securities.\textsuperscript{418} In order to inform itself, the Commission is entitled to a dossier which might be called a short registration statement, and such further information as it may request which may be useful to it.\textsuperscript{419}

Through its power to delay a license, or compel disclosure, or

\textsuperscript{412} Alamigeon, \textit{op. cit.} note 371 \textit{supra}, at 76.
\textsuperscript{413} Arrêté Royal No. 185 of July 9, 1935; for a full examination of this decree and the operations under it, see Ponlot, \textit{Le Statut Légal des Banques et le Contrôle des Emissions de Titres et Valeurs} (1958).
\textsuperscript{414} See the Report accompanying the decree, printed in Ponlot, \textit{op. cit. supra} note 413, at 314-324; see also O.E.E.C., \textit{The Supply of Funds for Industrial Development in Europe and the United States}, 35-36 (1957).
\textsuperscript{415} Arrêté Royal No. 185, July 9, 1935, arts. 28, 29.
\textsuperscript{416} Loss, \textit{Securities Regulation} 175-178 (1951).
\textsuperscript{417} Arrêté Royal No. 185, July 9, 1935, art. 28.
\textsuperscript{418} \textit{Id.} art. 29.
\textsuperscript{419} \textit{Id.} art. 27, 28.
both, the Commission has exercised a profound influence over many phases of corporation financial practice which have no immediate relation to public offerings. Believing that the purchase of treasury shares is a dubious practice, the Commission has induced one company to adopt provisions (presumably charter amendments) to prevent repetition; another company was induced to cancel treasury shares, to preclude reissue. Where affiliated companies had bought shares in each other, the Commission induced both to liquidate their holdings. Where shares are issued over par, the Commission requires that the surplus be placed in a reserve, unavailable for dividends.

The Commission has taken a very lively interest in profit-sharing plans of executive compensation, which have had great post-war popularity in Belgium. Many profit sharing plans are based, it appears, on the excess over some quantity of profit established many years ago, and now outdated by inflation or other factors. In these cases, the Commission believes that the compensation plan should be revised to raise the profit base above which the profit-sharing plan operates. Taking a leaf from American practice, the Commission has decided to require a listing of the compensation of the governing board members and top executives, with the compensation of each, and each one’s qualifications. However, the registration statement is not a public document, and the prospectus is not required to do more than show the total remuneration to the governing board members as a group.

The Commission engages in a host of other activities, none of which will amaze an American familiar with the activities of the S.E.C., but most of which are foreign to European practice. It requires the disclosure of underwriting arrangements and underwriting expenses. It requires disclosure that the company has paid a board member’s expenses of legal defense, or that board members have conflicts of interest with the corporation. In one case it influenced a company with subsidiaries to present a consolidated balance sheet—a rare practice in Europe. It has also introduced

420 Ponlot, op. cit. supra note 413, at 231, 232.
421 Id. 237.
422 Id. 235.
423 Id. 239-41.
424 Id. 264.
425 Id. 251-52.
426 Id. 255-56.
427 Id. 267. Officials of Esso-Standard (France) advised us that they had introduced a consolidated balance sheet in France in the late 1950’s, hoping that other companies would follow suit; but no others did.
the use of comparative profit and loss statements covering a period of years.\textsuperscript{428}

These items will suffice to show that the Banking Commission, with a relatively small staff and small statutory basis, has an influence in many directions which recalls securities regulation in Washington. The fact that it is alone in doing so will emphasize, at the same time, the absence of similar securities regulation in the other countries of the market.

E. A Common Market for Capital?

Our dominant impression, as we look at the prospects for European investment, is very different from our impression of the prospects for trade in commodities. For commodities, we envision by 1970 a truly common market, in which the same kinds of typewriters will be sold and used in Hamburg as in Palermo, with no more difference in price than the cost of commercial freight. They cannot be scarce in Amsterdam and plentiful in Venice, nor can the available kinds and qualities vary greatly.

The capital markets are quite different. We start out with different company laws, which limit the kinds of securities which companies can issue. German and French companies can make the same kinds of typewriters, but German limited liability companies can issue bonds, while French cannot. French stock companies’ preferred stock must have voting rights, but German need not. Besides, even the tastes of investors have changed; French investors demand inflatable bonds; Germans and Belgians will (to a greater extent) accept fixed interest.

The prospects are also different. While there is a definite schedule for eliminating customs and quotas at an arithmetic rate,\textsuperscript{429} there is no such formula for eliminating barriers to capital movement. There is not even a firm promise to eliminate them entirely, but only “to the extent necessary for the proper functioning of the Common Market.”\textsuperscript{430} These weasel words invite wide differences of opinion as to what kind of functioning is “proper” in the capital markets; if such differences had not existed, it would not have been necessary to use such weasel words.

Although the nations pledge themselves to “co-ordination of exchange policies,”\textsuperscript{431} they say nothing about the licensing of investment offerings, except what may be implicit in the promise to

\textsuperscript{428} Id. 270–71.
\textsuperscript{429} Treaty arts. 12–17, 30–37.
\textsuperscript{430} Id. art. 67.
\textsuperscript{431} Id. art. 70(1).
“approximate” laws of all kinds which “distort the conditions of
competition.” 482 We must therefore reconcile ourselves to a long-
term continuance of the present diversity of the measures and
policies of regulation.

However, diversity alone need not block the development of an
international market. There is an interstate market for capital
in the United States, despite the rigors of, and the irrational dif-
fences between, the blue sky laws of Illinois and Michigan. It
exists partly because the companies can escape to Delaware, and
the money can escape to New York, where the requirements of only
one state and of the federal government must be met.

To draw a parallel in Europe, we might ask whether European
investors’ money can escape to Luxembourg—a country of notorious
freedom from exchange regulations, and whether companies which
operate in Italy, Germany, and Belgium would turn to this market
for money on similar terms of investment?

To answer this question, we will start by saying that we think
that to some extent this is already happening. The curtain of ex-
change control is not a curtain of iron, and it will become less and
less effective as commerce among the nations of the Market expands.
An official of the Belgian Banking Commission told us that he
thought the Commission’s controls were evaded in a number of
cases by investments effected in Luxembourg; this is particularly
easy, because there is no exchange control at all between these two
countries. (They have a monetary union.)

But we think that the growth of a Community-wide capital market
will be very slow, and will depend on the solution of many problems
which are not envisaged by the Treaty of Rome. There will first
have to be a unanimous desire, which evidently did not exist when
the Treaty was signed, to establish a common capital market. Next,
there will have to be a total and permanent relaxation of exchange
controls.

Before that will come to pass, we think there will have to be a
general agreement on what kinds of controls over investment are
necessary and proper, and there will have to be confidence among
the investors of the various countries that the investments available
in other countries are as safe as those in their own. This kind of
confidence is not likely to arise until similar controls, or common
controls, exist in the various countries. Perhaps this will come about
through “approximation of laws.” But an American finds it difficult

482 Id. art. 101.
to imagine uniformity in investment standards without the existence of an interstate agency with direct regulatory powers, like the Securities Exchange Commission. Since the Treaty of Rome does not provide even a skeleton for such regulation, a European common capital market as Americans know it appears to be along way off.

For the American businessman, this means that if he wants to raise money in Europe, he will probably have to raise it in the country where he plans to use it. Even though some of the ultimate investors may reside in other countries, the money will be raised according to the usages and regulations of the country where the industrial operation is located. Hence the choice of site of operation will be made with an eye on investment conditions as well as on merchandise and labor markets.

A good location, from a financial point of view, is one in which investment capital is fairly plentiful, the usual investment media (e.g. convertible bonds, fixed interest bonds) are acceptable, and in which money once invested, and its profits, can be freely withdrawn and invested in other countries of the Community, or returned to the United States. The choice is the more difficult to make because it depends on future controls, rather than present ones. According to common knowledge, Belgium and Luxembourg have enjoyed the longest monetary stability (since 1946), with accompanying freedom of exchange control. Germany has been in the same group since about 1950. Netherlands currency has been stable, but exchange control has been fairly tight. Italy and France, in that order, have most recently attained monetary stability, and have the strictest currency controls today. The investor must guess what the respective advantages of the various countries will be tomorrow.

**POSTSCRIPT**

The lawyer's job in planning a business operation—whether foreign or domestic—may be thought of as involving two parts: conception and communication. The lawyer must first form a mental picture of the company structure that he wants to set up, and of the roles which the various officials will play, individually and in relation to each other. Next, he must somehow communicate these ideas to the officials who are to do the acting.

On the domestic scene both parts of the job may be carried out almost unconsciously, because the lawyer conceives of a structural
pattern which is completely traditional, and anyone who is named as president of a parent company, or president of a domestic subsidiary, has the same conception as the lawyer of how he is supposed to act.

When the American lawyer turns to a foreign business operation, both processes are greatly complicated. The complication of the communication process is obvious. An American “director” is not the equivalent of an Italian dirreitore. Even if the “director” is equated with the more nearly comparable amministratore, the problem is not solved, because the amministratore also thinks of himself rather differently than does an American “director.”

But the difficulty is one of conception as well as of communication. The European institutions, and the roles which people play within them, are just a little different from the institutions which exist, and the roles which are played, in the United States. The American lawyer is in the position of a composer writing music for people who not only use a different system of musical notation but also play different instruments on different scales than those which he knows.

Many American lawyers—of necessity—probably ignore these differences. They make their plans in terms of Delaware certificates of incorporation, Delaware boards of directors, and Delaware capital and surplus. Their instructions may be quite impossible of execution within a foreign legal system. Most of this impossibility will go undetected on both sides, because the faithful foreign agents will carry out (in Italian) whatever seems to them the most plausible interpretation of the American wishes. They will then report their action (in English) in the terms of the instructions.

So long as this system works, there is no reason to change it. It probably is much better than it would be if the American lawyers succeeded in recreating on the Italian scene a corporate structure duplicating precisely the one in Detroit.

But the stiffer competition of the emerging Common Market is likely to demand something better. American enterprises will reach their full potential only if some of their management know-how is effectively transferred to Europe, and if errors in management are efficiently located and corrected. This means that the American lawyer who bears responsibility for the organization of a European business operation needs to know—like a composer—something about the musicians who will perform his piece, the instruments they play, and the notations which they recognize. Learning these
things is an endless task, and the American lawyer will never know them all. But every bit that he learns about the laws and the institutions of Common Market countries will contribute a little to his ability to design and control the Common Market operations of an American enterprise.