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FORMING A SUBSIDIARY IN THE EUROPEAN COMMON MARKET*

Alfred F. Conard†

THE appearance of a new market which is open to free enterprise and contains almost as many customers as the United States has opened immense opportunities to American enterprises, with their unique experience in mass production and mass marketing.¹ General counsel for large American enterprises are confronted with a new need for some understanding of the problems of organizing subsidiary companies² in this new market. The present article is written to supply an introduction to the legal factors which bear on solutions of these problems.³

* This is part of a chapter from the second volume of *American Enterprise in the Common Market: A Legal Profile*, which is to be published later this year in the Michigan Legal Studies. It is edited by Professor Eric Stein and by Thomas L. Nicholson, Esq., of the Chicago Bar.

† Professor of Law and Director of Graduate Studies, University of Michigan Law School. The author acknowledges with gratitude the assistance of a large number of European collaborators who answered questions, and read the manuscript in whole or in part; some of the opinions expressed in the article are based on the views of these collaborators. The collaborators include: for Belgium, Professor J. Heenen; for France, Professor R. Houin; for Germany, Professor R. Serick; for Italy, the late Professor T. Ascarelli, Dr. Bruna, and Professor Bernini; for Luxembourg, Mr. E. Arendt; and for the Netherlands, Mr. Deelen and Mrs. van Vlis.

¹ See AMERICAN MANAGEMENT ASSOCIATION, *THE EUROPEAN COMMON MARKET* (1958); COMMITTEE FOR ECONOMIC DEVELOPMENT, *THE EUROPEAN COMMON MARKET* (1959).

² I use the term "company" here and elsewhere to designate any of the forms of business association extant in the Common Market countries which would serve American purposes, including the broad range of forms signified by the French *société*, the German *Gesellschaft*, the Italian *società*, or the Dutch *vennootschap*. I do not use the term "subsidiary corporation" at this point because a few writers have chosen to identify the word "corporation" with only one of the available European business forms—the *société anonyme*, *Aktiengesellschaft*, *società per azioni*, or *naamloze vennootschap*. See especially FRIEDMAN AND PUGH, *LEGAL ASPECTS OF FOREIGN INVESTMENT* ix, *passim* (1959). To speak at this point only of "subsidiary corporations" would therefore imply exclusion of an alternative business form which is preferable in many cases—the *société à responsabilité limitée*, *Gesellschaft mit beschränkter Haftung*, *società a responsabilità limitata*, or *personen-vennootschap met beperkte aansprakelijkheid*.

Further comment on the terminological problem appears in another part of the text, and in notes 17 to 20 *infra*.

³ This article is directed to a reader who has already decided that the formation of a European subsidiary is appropriate to his business needs. The difficult questions of whether a particular investor should form any subsidiary in the Common Market and, if so, whether he should form one or several, horizontally or in tiers, are discussed in the author's chapter of the forthcoming STEIN AND NICHOLSON, *AMERICAN ENTERPRISE IN THE COMMON MARKET: A LEGAL PROFILE*, but the discussion is omitted from the present article.

I. THE COMPANY LAWS OF THE COMMON MARKET

The lawyer who plans to organize a Common Market subsidiary must first acquire some acquaintance with the company laws which are in force there. For the six countries of the Market⁴ there are six systems of company law—all different. And there are not six, but *eight* sets of 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, the lawyer will find that four languages cover all eight of the texts. These are French, German, Italian, and Dutch (Flemish being a dialect of Dutch). Furthermore, a knowledge of the French language will permit the reader to examine official texts of three countries (France, Belgium, and Luxembourg), and translated texts, with latest amendments, of the other three.⁵ Complete texts of the relevant laws, with latest amendments, will probably be available soon in German as well.⁶ There are also recent English translations available for the Dutch and Italian laws, although there are no English language services to keep them up-to-date.⁷

The list of company laws in the Common Market may be lengthened within a few years by a new company law, which would be uniform throughout the six countries. An enterprising committee of Frenchmen is now studying this possibility.⁸ But the movement in this direction is purely voluntary and unofficial.

⁴ Belgium, France, Germany, Italy, Luxembourg, and Netherlands.

⁵ 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 MARCHÉ 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.

⁶ 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.

⁷ *Italy*: An English translation of Italian company law was published in 1957 by Mediobanca of Milan, under the title *THE AMERICAN INVESTORS' DIGEST OF ITALIAN CORPORATE LAW*.

Netherlands: *INTERNATIONAAL JURISDISCH INSTITUUT, NETHERLANDS LEGAL PROVISIONS ON COMPANIES LIMITED BY SHARES* (1957); *VAN DER MEER, DUTCH CORPORATION LAW* (1959). The *Instituut* publication is generally in British idiom; Van der Meer, in American.

⁸ A congress to consider adoption of a "European" company law was held at Paris in June 1960 under auspices of the Order of Advocates of Paris, and agreed on a number of points. Their proceedings have been published as a supplement to *Revue du Marché Commun*, No. 27 (July-Aug. 1960).

Although the Common Market Treaty obliges the Community members to seek conformity of legislation on several subjects, company law is not on the list.⁹

A. *Family Resemblances and Divergencies*

Fortunately for the American lawyer, all of the six company law systems reveal strong family resemblances, as seen from an American perspective. One discovers many concepts which are common to the six countries, although seldom met in any of the fifty American states. All six legal systems share basic concepts which were enunciated in the Napoleonic Civil and Commercial Codes. The company laws of Luxembourg, Belgium, and Italy also reflect a strong influence of the French Stock 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 become accustomed within the hospitable boundaries of Delaware.

B. *The Official Sources*

When the lawyer decides to go behind the various paraphrases and translations of Common Market company laws, and to consult the official texts, he meets a confusing variety of arrangements. The common generalization that European law (unlike American) is "codified" applies to the law of business companies in only three of the six countries—Belgium, Italy, and Netherlands. In Belgium and Netherlands, the company law is a part of the commercial codes, which collect a large body of law applying to all kinds of

⁹ The Treaty Establishing the European Economic Community (1957) obliges the signatories to "co-ordinate" their legislation with regard to police, security, and health regulations on foreigners [art. 56 (2)], their legislation on entry of foreigners into business [art. 57 (2)], and their exchange control policies [art. 70 (1)]. They also promise to *negotiate* about mutual recognition of companies, transfer of nationality of companies, and international mergers. But the laws under which companies are formed and operate are not included unless they are among the laws having "a direct incidence on the . . . functioning of the Common Market" which are to be "approximated" (art. 100).

business transactions.¹⁰ Belgian and Dutch lawyers, referring to company laws, cite "Commercial Code, Book I, Title IX, article 60," or "Commercial Code, article 36a." In Italy, the company law is incorporated in the *Civil* Code; this is likely to surprise a lawyer with extensive foreign experience, who has learned that in twenty or thirty other countries a civil code citation is never a reference to the law of business companies. He may be even more surprised to find the citation, when he tracks it down, in the code division on "Labor Law."¹¹

Of all the countries, France has the most uncoded collection of company laws, reflecting vicissitudes of national history almost as picturesquely as the architectural face of Paris.¹² 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 on companies in the Code of Commerce (Articles 18-46). For specific questions of French company law one must usually turn to uncoded statutes; the principal ones discussed here will be called 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 that one encounters laws which certainly modify the effects of the law of 1867, but are not framed as amendments to it and must be separately cited.

¹⁰ *Belgium*: CODE DE COMMERCE, LIVRE I, Titre IX; WETBOEK VAN KOOPHANDEL, Book I, Titel IX (hereinafter cited as C. Com. I-IX, or W.K. I-IX, respectively). *Netherlands*: WETBOEK VAN KOOPHANDEL, art. 15-56h (hereinafter cited as W.K.)

There are, of course, general principles applicable to companies in many parts of the civil codes, especially in the parts on contracts of association. There are also special corporation acts, like the Netherlands act on cooperative associations, which are not integrated. The statement in the text applies to a set of rules on business corporations which is approximately as comprehensive as for instance, the American "Model Business Corporation Act."

¹¹ The company laws, ordinarily cited merely by section of the Civil Code (for instance, *Codice Civile*, art. 2397), are arranged as Title V (*Delle società*) of Book V (*Del lavoro*). The merger of the commercial code in the civil code is a step which has been widely discussed and advocated in other European countries. The incorporation of company law into labor law is an oddity of the fascist period, in which the codes were revised (1942). This unusual arrangement seems to have no effect on the content of the company laws, or on their interpretation.

¹² See Houin, *Reform of the French Civil Code and the Code of Commerce*, 4 AM. J. COMP. L. 485 (1955).

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.

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 *HBG*), but the Luxembourg laws are available only in a separate booklet.¹³

For the benefit of readers who have some familiarity with the official texts, I list below the official names of the principal company laws, followed by the English nickname which I will use in the text, and by the abbreviated citation used in the footnotes of this article.

<i>Country</i>	<i>Cited in country of origin as:</i>	<i>English nickname</i>	<i>Citation herein</i>
Belgium	Code de Commerce, Liv. I, Tit. IX; Wetboek van Koophandel, Boek I, Tit. IX	Code of Commerce Book I, Title IX	C. Com. I-IX
France	Loi du 24 juillet 1867, sur les sociétés	Stock Company Law	Law of 1867
	Loi du 7 mars 1925, tendant à instituer des sociétés à responsabilité limitée	Limited Liability Company Law	Law of 1925
Germany	Gesetz über Aktiengesellschaften und Kommanditgesellschaften auf Aktien (“Aktengesetz”)	Stock Company Law	AktG

¹³ RECUEIL DES LOIS CONCERNANT LES SOCIÉTÉS COMMERCIALES (1956).

	Gesetz betreffend die Gesellschaften mit beschränkter Haftung (GmbH Gesetz)	Limited Liability Company Law	GmbHG
Italy	Codice Civile, art. 2247-2574	Civil Code, art. 2247-2574	C. Civ.
Luxembourg	Loi du 10 août 1915 concernant les sociétés commerciales; Gesetz vom 10 August 1915, betreffend die Handelsgesellschaften ¹⁴	Company Law	Company Law
Netherlands	Wetboek van Koophandel, art. 15-56h.	Code of Commerce art. 15-56h	W.K.

II. THE CHOICE OF COMPANY FORM

A. *Two Kinds of "Corporations"*

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 of organization bear witness to the European legislators' desire to provide separate legal structures for those 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, and enjoys relative privacy.¹⁵ In these respects, the European dichotomy ap-

¹⁴ 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.

¹⁵ An English language introduction to the limited liability company in various European countries may be found in the following articles: Eder, *Limited Liability Firms Abroad*, 13 U. PITT L. REV. 193 (1952); Israels and Taubenblatt, *The Close Corporation in Foreign Law*, STATE OF NEW YORK, REPORT OF THE LAW REVISION COMMISSION 416 (1948); Schneider, *The American Close Corporation and its German Equivalent*, 14 BUS. LAW. 228 (1958); Treillard, *The Close Corporation in French and Continental Law*, 18 LAW & CONTEMP. PROB. 546 (1953).

pears much like the one which American writers have increasingly drawn in recent years.

But the American dichotomy is a differentiation of fact — a difference in how the shares are actually held and traded. Legally, both kinds of American companies ("close" and "publicly-held") belong to the same legal category ("business corporation" or "corporation 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 instance, the Delaware General Corporation Act, 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.¹⁶

In Europe, on the other hand, these two kinds of companies belong to different legal categories, add different words or initials to their corporate names, and are formed under different statutes. To pass from one form to the other requires the adoption of a completely new charter, through a procedure called "transformation."

The Netherlands are 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 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.

B. *What To Call Them — in English*

In order to write in English about legal institutions which do not exist in English-speaking countries, one must make some arbitrary choices of terminology. I shall use just two terms — "stock

¹⁶ 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 (1929). Rutledge, *Significant Trends in Modern Incorporation Statutes*, 22 WASH. U.L.Q. 305, 338-9 (1937); Fuller, *The Incorporated Individual: A Study of the One-Man Company*, 51 HARV. L. REV. 1373, 1406 (1938); Winer, *Proposing A New York "Close Corporation Law"*, 28 CORNELL L.Q. 313 (1943); O'Neal, *A Plea for Separate Statutory Treatment of the Close Corporation*, 33 N.Y.U.L. REV. 700 (1958).

company" and "limited liability company" to describe the two principal kinds of commercial companies which exist in the six Common Market countries, under the various names listed below.

"Stock Company"

"Limited Liability Company"

Belgium:

(French) *société anonyme* (SA)

société de personnes à responsabilité limitée (SPRL)

(Flemish) *naamloze vennootschap* (NV) *personenvennootschap met beperkte aansprakelijkheid*

France:

société anonyme (SA)

société à responsabilité limitée (SARL)

Germany:

Aktiengesellschaft (AG)

Gesellschaft mit beschränkter Haftung (GmbH)

Italy:

società per azioni (SpA)

società a responsabilità limitata (SARL)

Luxembourg:

(French) *société anonyme* (SA)

société à responsabilité limitée (SARL)

(German) *anonyme Gesellschaft* (AG)

Gesellschaft mit beschränkter Haftung (GmbH)

Netherlands:

naamloze vennootschap (NV)

The terms which I have chosen are used by a number of other writers on foreign law,¹⁷ and have the additional advantage that they are literal, or nearly literal translations of the originals. The only important departure from literalness is made for terms which

¹⁷ The following incomplete bibliography on others' usages may be of some interest: "Limited Liability Company" (for SARL - GmbH): FRIEDMANN et al., *LEGAL ASPECTS OF FOREIGN INVESTMENT* (1959).

"Stock company" (for SA - AG): Eder, *Spain: New Law of Stock Companies*, 1 AM. J. COMP. L. 117 (1952); Eder, *Spain: Law of Stock Companies*, 2 AM. J. COMP. L. 234 (1953).

"Limited Liability Firm" (for SARL - GmbH): Eder, *supra* note 15; Eder, *Colombia: Control of Limited Liability Firms*, 2 AM. J. COMP. L. 70 (1953); Eder, *Venezuela: Commercial Code*, 5 AM. J. COMP. L. 628 (1956).

"Close Corporation" (for SARL - GmbH): Reverdin and Homburger, *The American Close Corporation and its Swiss Equivalent*, 14 BUS. LAW. 263 (1958); Israels and Taubenblatt, *supra* note 15, at 416.

"Corporation" (for SA - AG): FRIEDMANN et al., *LEGAL ASPECTS OF FOREIGN INVESTMENT* (1959); but cf. FRIEDMANN et al., *THE PUBLIC CORPORATION* (1954).

"Public companies and private companies" (for SA - AG and SARL - GmbH, respectively): Treillard, *supra* note 15, at 546.

if literally translated would be "nameless company" (*société anonyme*, *anonyme Gesellschaft*, and *naamloze vennootschap*).

The terminology used here should cause no confusion, except for readers who, by reason of previous indoctrination, believe that one of the European forms—usually the *société anonyme*—is the equivalent of the American "corporation." Such readers are doomed to a good deal of confusion, regardless of what terminology is used here. For the American "corporation" embraces many institutions—public and private, profit and non-profit—which are quite beyond the scope of any of the European company forms. Further, the use of "corporation" for *société anonyme*, but not for the *société à responsabilité limitée*, implies that the one is somehow more corporate than the other. Any such implication is quite false. Both are equally entities, and both equally confer limited liability upon their members. Finally, the use of "corporation" to translate *société anonyme* leaves us without any appropriate word to translate the French *corporation*, the Italian *corporazione*, the Dutch *corporatie*, and the German *Körperschaft*, all of which have a broad connotation like the American "corporation" in its wider usages.

C. Other Forms of Business Association

Of course there are many kinds of business associations used in Common Market countries in addition to the stock company and limited liability company. In each country there are partnerships¹⁸ and limited partnerships,¹⁹ just as in the United States.

¹⁸ Partnerships:

Belgium: *Société en nom collectif* (*vennootschap onder gemeenschappelijke naam*), C. Com. I-IX, arts. 15-17.

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

France: *Société en nom collectif*, C. Com., arts. 20-22.

Italy: *Società in nome collettivo*, Codice Civile, arts. 2291-2312 (hereinafter cited as C. Civ.).

Luxembourg: *Société en nom collectif*—*offene Handelsgesellschaft*, *loi du 10 août 1915, concernant les sociétés commerciales* (hereinafter cited as Company Law), arts. 14-15.

Netherlands: *Vennootschap onder eene firma*, W.K., arts. 16-18.

¹⁹ Limited Partnerships:

Belgium: *Société en commandite simple* (*vennootschap bij wijze van enkele geldschieting*), C. Com. I-IX, arts. 18-25.

Germany: *Kommanditgesellschaft*, HGB, §§161-177.

France: *Société en commandite*, C. Com., arts. 23-28.

Italy: *Società in accomandita semplice*, C. Civ., arts. 2313-2324.

Luxembourg: *Société en commandite simple* (*einfache Kommanditgesellschaft*), Company Law, arts. 16-22.

Netherlands: *Vennootschap bij wijze van geldschieting* (or *vennootschap en commandite*), W.K., arts. 19-35.

There is also in each of the countries a "limited partnership with shares,"²⁰ and there are a number of special purpose companies, such as mutual insurance companies, co-operative associations and credit unions.

None of these business associations seems likely to be of much interest to American traders and investors. Co-operatives 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 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.

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 Limited 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.²¹ However, the number of American enterprises which would wish to participate in a European limited partnership would be very small, and this article will not give further attention to it.

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

²⁰ The organizations referred to resemble limited partnerships in that some members are liable for firm debts, while others are not; they differ from limited partnerships, however, 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:

Belgium: *Société en commandite par actions* (*Vennootschap bij wijze van geldschieting op aandelen*), C. Com. I-IX, arts. 105-115.

France: *Société en commandite par actions*, Law of July 24, 1867, arts. 1-20.

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

Italy: *Società in accomandita per azioni*, C. Civ., arts. 2462-2471.

Luxembourg: *Société en commandite par actions* (*Kommanditgesellschaft auf Aktien*) Company Law, arts. 102-112.

Netherlands: *Commanditaire vennootschap op aandelen*, W.K., arts. 19-21.

²¹ See Crane, *Are Limited Partnerships Necessary?* 17 MINN. L. REV. 351 (1933).

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.²²

D. *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.²³ 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 3½ to 1, and was apparently even higher in Germany.²⁴ Although many of the reasons why Europeans might prefer the limited liability company do not apply to Americans, this form deserves more consideration than it has commonly received. Its unpopularity among Americans may result partly from the fact that it looks strange and unfamiliar. I 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.

1. *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

²² 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.

²³ A casual survey of well-known American subsidiaries in Europe has revealed no limited liability companies except in Germany. In that country, General Motors and Standard of New Jersey have German subsidiaries which are stock companies, and subsidiaries which are limited liability companies; *Frigidaire GmbH* is a subsidiary of *Adam Opel AG*, which is a subsidiary of General Motors; *Vereinigte Asphalt und Teerproduktion Fabriken GmbH*, is a subsidiary of *Esso AG*, which is a subsidiary of Jersey Standard. *MOODY'S INDUSTRIAL MANUAL* 2734, 1648 (1959). 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).

²⁴ *RECUEILS PRATIQUES DU MARCHÉ COMMUN*, vol. 1, 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. In Western Germany figures of companies in existence in 1955 showed 34,254 GmbH against 3060 AG. *REC. PRAT. DU M.C., Indications pratiques*, for Germany.

claimants.²⁵ In Italy, stock companies no longer issue bearer shares, but registered shares are considered "negotiable" just as in the United States.²⁶ Limited liability companies' shares are never considered negotiable; they must always be transferred on the books of the company;²⁷ in Germany the transfers must even be notarized;²⁸ in Italy, no certificates of ownership are issued.²⁹ The buyer of a limited liability company share (with or without a certificate) takes it subject to any adverse claim of title, any claim of the company for unpaid share subscriptions, and any restrictions on transfer, to which the transferor was subject.

In some, but not all, countries, there are further impediments to 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.³⁰ This provision puts a minority shareholder at the mercy of the controlling group when he decides to sell. It is one of the factors which cause Frenchmen to form a stock company rather than a limited liability company, even when they intend it to be closely held. In Germany and Italy, there is no rule requiring consent to transfer unless it is voluntarily inserted in the corporate charter.³¹

2. *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

²⁵ *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.

²⁶ 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 March 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.

²⁷ *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*: C. Civ., art. 2479 (transfer ineffective until registered); *Luxembourg*: Company Law, art. 190 (transfer incomplete until the company is formally notified).

²⁸ *Germany*: GmbHG, §15, ¶3.

²⁹ *Italy*: C. Civ., art. 2472.

³⁰ *Belgium*: C. Com. I-IX, art. 126; *France*: Law of 1925, art. 22; *Luxembourg*: Company Law, art. 189.

³¹ *Germany*: GmbHG, §15, ¶5 (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).

traded on the securities markets. Some of the countries have a specific prohibition against public issue or trading.³² 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, previously explained, is the one on issuing negotiable shares. A further prohibition, effective in Belgium, France, Italy, and Luxembourg, prohibits the public issue of bonds.³³

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 or, 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,³⁴ the inhibition on public bond issues will probably not make much practical difference to a company until it becomes very large and well-known.

3. *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.³⁵ According to Professor Heenen of Brussels (my Belgian collaborator) this is a rule of substance, not to be evaded by use of dummy shareholders. 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 percent

³² *Luxembourg*: Company Law, art. 188; *France*: Law of 1925, arts. 4, 37.

³³ The prohibition is variously phrased. In France and Luxembourg, it is directed against "public issues" of all kinds. *France*: Law of 1925, art. 4; *Luxembourg*: Company Law, art. 188. In Belgium and Luxembourg, it is simply a prohibition against issuing "obligations," which is construed to forbid the type of obligations bought by investing public, not the type taken by banks. *Belgium*: C. Com. I-IX, art. 131; *Italy*: C. Civ., art. 2486.

³⁴ The decline in private lending through bonds is discussed in another section of the chapter which will appear in *American Enterprise in the Common Market*. The reasons are complex; one is investors' fear of inflation; another is the wiping out by past inflation of the family fortunes, endowments, and insurance reserves which would otherwise be invested in bonds.

³⁵ C. Com. I-IX, art. 119.

basic tax (before the progressive surtax) instead of the 5 percent 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 my collaborators view this problem as temporary. When it is solved, the Italian limited liability company may be a relatively attractive form of enterprise.

Some of my European collaborators report that the limited liability company is viewed with suspicion by creditors because it has been used so often for under-capitalized enterprises which eventually failed; the stock company on the other hand enjoys a presumption of financial responsibility. But I suppose 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.

4. *Restrictability of Share Transfers.* Restrictions on transfer were listed above 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 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.³⁶ In Italy and Germany, the law does not impose this restriction, but permits its insertion in the company charter.³⁷

It is true that some degree of non-negotiability is also attainable in stock company shares. Professor Houin believes that a numerical majority of French stock companies would be found to have some rules restricting stock transfer. But restrictions on transfer are not expressly authorized by the stock company laws of all countries,³⁸ and the extent to which transfers may be validly restricted is not clearly defined either by case law or by legal theory.³⁹

5. *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,⁴⁰ while a limited liability company requires only two.⁴¹ 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 each one need not hold more than one share; and they may be bound by contract to assign the share to someone else on demand of the parent company.⁴²

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).⁴³ Since a shareholder's

³⁶ Note 30 *supra*.

³⁷ Note 31 *supra*.

³⁸ Germany expressly authorizes charter restrictions on transfer of stock company shares: AktG, §61 (3). But many desired forms of restriction are beyond the statutory authorization. See SCHLEGELBERGER-QUASSOWSKI, KOMMENTAR ZUM AKTIENGESETZ §71, Anmerkung 9 (1939).

³⁹ An interesting exchange of views on the subject in Belgium is contained in a pair of comments by Coppens, 64 JOURNAL DES TRIBUNAUX 215 (1949), and de Rouvreux, 55 REVUE PRATIQUE DES SOCIÉTÉS CIVILES ET COMMERCIALES 54 (1956). Cf. VAN RYN, PRINCIPES DE DROIT COMMERCIAL, Part I, 364 (1954). For Germany, see Schneider, *supra* note 15, at 233.

⁴⁰ Belgium: C. Com. I-IX, art. 29; France: Law of 1867, art. 23; Luxembourg: Company Law, art. 26.

⁴¹ Belgium: C. Com. I-IX, art. 119; France: Law of 1925, art. 5; Luxembourg: Company Law, art. 183.

⁴² Cf. Lepaulle and Jeantet in FRIEDMANN et al., LEGAL ASPECTS OF FOREIGN INVESTMENT 214, 220-221 (1959).

⁴³ *Ibid.*

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, 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 reduced 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.⁴⁴ 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.⁴⁵ In Germany, there is a difference in the number of incorporators required (five in the stock company; two in the limited liability company),⁴⁶ but there is no objection to 100 percent ownership by a single shareholder after the company is once formed.⁴⁷ Hence the selection of the extra incorporators does not demand much attention in either Germany or Italy. The Netherlands have no limited liability companies, but two incorporators are enough to form a stock company, and the number of shareholders after incorporation need not exceed one.

6. *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.⁴⁸ It is not even necessary to

⁴⁴ C. Civ., art. §2247.

⁴⁵ *Id.*, art. 2362.

⁴⁶ AktG, §2: five members; GmbHG, §2: specifying no number, but implying plurality.

⁴⁷ BAUMBACH-HUECK, AKTIENGESSETZ, Anhangnach §15 (9th ed. 1956).

⁴⁸ *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 (*conseil 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 §77, Oct. 11, 1952. The single manager is called a *Geschäftsführer*.

Italy: C. Civ., art. 2487. But an auditing committee (*collegio sindacale*) is required if the capital is over 1,000,000 lire (about \$1,500). *Id.*, art. 2488. The single manager is called an *amministratore unico*.

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.⁴⁹

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 stock company must have a supervisory board (*Aufsichtsrat*) of three or more members who are not themselves executives of the company, but who elect one or more other persons to an executive board (*Vorstand*).⁵⁰ In other words, the investor in a stock company must find three policy-makers whom he trusts enough to put 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*).⁵¹ 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, likewise, four persons must be found to fill the necessary positions—three managers (*administrateurs, beheerders*) and at least one auditor (*commissaire, commisaris*).⁵² The directors may be employees of the company, but the auditors must be strictly independent—not employed by the managers or by the company, and not related by blood or marriage, to the managers.⁵³ The requirements are the same in Luxembourg except

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 *Geschäftsführer*.

⁴⁹ *Belgium:* C. Com. I-IX, art. 129; *France:* Law of 1925, art. 24; *Germany:* GmbHG, §6; *Italy:* C. Civ., arts. 2487 and 2383; *Luxembourg:* Company Law, art. 191.

⁵⁰ AktG, §§70, 86, 90.

⁵¹ C. Civ., arts. 2380, 2397, 2399.

⁵² *France:* Law of November 16, 1940, art. 1 (managers); Law of 1867, art. 32 (auditors); *Belgium:* C. Com., I-IX, arts. 55 and 64.

⁵³ *France:* Law of 1867, art. 33; *Belgium:* C. Com. I-IX, art. 64, *quater* (as amended by law of Dec. 1, 1953).

that there are no statutory prohibitions of family or business relationships between the auditor and the company or its managers.⁵⁴

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 one million lire (about \$1500); above that, auditors are required.⁵⁵ In Germany, the line is drawn at 500 employees; with more, a three-man supervisory board is required.⁵⁶ 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.⁵⁷ Only 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 (*Vorstand*) in a German stock company, and perhaps the manager (*gérant*) in a French limited liability company, cannot be removed from their position without proof of unfitness for the office.⁵⁸ Most officers, including the members of the governing boards in France and Germany (*conseil d'administration*, *Aufsichtsrat*), are removable at the pleasure of the shareholders.⁵⁹ 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.

7. *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 mem-

⁵⁴ *Luxembourg*: Company Law, art. 61.

⁵⁵ C. Civ., art. 2488.

⁵⁶ *Betriebsverfassungsgesetz*, §77 (hereinafter cited as *BetrVerfG*).

⁵⁷ *Belgium*: C. Com. I-IX, art. 134; *France*: Law of 1925, art. 32.

⁵⁸ *France*: Law of 1925, art. 24, but case law has permitted some modification by provision in the articles; *Germany*: *AktG*, §75 (3).

⁵⁹ *Belgium*: C. Civ., I-IX, art. 53; *France*: Law of 1867, art. 22; *Germany*: *AktG*, §87 (3); *Italy*: C. Civ., art. 2383; *Netherlands*: W.K., art. 48b.

bers (who choose the executives) must be labor representatives. This requirement does not affect limited liability companies until they have 500 or more employees.⁶⁰

8. *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, for example, stock companies must publish their annual financial statements,⁶¹ 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.

9. *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.⁶² Another is the simplicity of the papers to be drawn up; 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 pricks in relation to the major expenses and difficulties inherent in a transatlantic plunge.

C. 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."⁶³ Like incorporation, it involves

⁶⁰ BetrVerfG, §77. "Family-owned" stock companies are exempted from the labor representation requirement, regardless of number of employees.

⁶¹ 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, 1959; J.O. Feb. 8, 1959, p. 1754; L'ACTUALITÉ JURIDIQUE 1959. III. 62.

⁶² 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 \$1,500) for a stock company and 50,000 lire (about \$75.00) for a limited liability company. C. Civ., arts. 2327, 2474.

⁶³ Belgium: The procedure is nonstatutory. France: Law of 1925, art. 41 (*transformation*); Germany: AktG, §§263-277 (*Umwandlung*); Italy: C. Civ., art. 2498 (*trasformazione*); Luxembourg: Procedure is non-statutory.

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 percent of the assets pass in exchange for stock in the new company, and that the 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 in 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.

III. THE CHOICE OF A STATE OF INCORPORATION

A. *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.⁶⁴

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 of each country, which provides that the articles must designate a central office (*siège, Sitz, sede, zetel*) which, at least inferentially, must be in that country.⁶⁵ In this respect they differ from the Delaware corporation act, which requires designation only of "its principal office . . . in this State,"⁶⁶ or the Illinois act, which calls for "the address . . . of its initial registered office in this State."⁶⁷ 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.⁶⁸ A few contemporary writers have questioned whether there are really any serious consequences to be feared,⁶⁹ and a Dutch authority declares that the Dutch Minister of Justice often ignores known violations of the rule.⁷⁰ The Italian law specifically permits a company to adopt, by *amendment* of its charter, a foreign central office.⁷¹ But in countries 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

⁶⁴ I adopt for use in comparative law the term employed by 2 RABEL, *THE CONFLICT OF LAWS* 31 (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.

⁶⁵ 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 "central office," in terms which leave no doubt that a court or registry in the country of the legislator is intended. See, for example: *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.

⁶⁶ Del. Gen. Corporation Law, DEL. CODE ANN., §102 (a) (2) (1953). The wording admits the possibility of other "principal offices" in any number of other states.

⁶⁷ Illinois Business Corporation Act, §47b, ILL. STAT. ANN. (Smith-Hurd, 1954), §157.47 (b).

⁶⁸ RIPERT, *TRAITÉ ÉLÉMENTAIRE DE DROIT COMMERCIAL* 268 (1954); VON GODIN-WILHELM, *AKTIENGESETZ*, §5, Anmerkung 6 (1937); KOLLEWIJN, *AMERICAN-DUTCH PRIVATE INTERNATIONAL LAW*, No. 3 *Bilateral Studies in Private International Law* 16 (1955). Kollwijn is somewhat skeptical of this view, but recognizes it as "prevailing."

⁶⁹ See BEITZKE, *JURISTISCHE PERSONEN IM INTERNATIONAL PRIVATRECHT UND FREMDENRECHT* 104 (1938).

⁷⁰ See KOLLEWIJN, *op. cit. supra* note 68, at 16.

⁷¹ C. Civ., art. 2437.

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.⁷² This seems to mean the actual central office, not a fictitious one stated in the articles. Under the prevailing American rule the corporation's existence and internal affairs are governed by the state of incorporation, wherever it may establish its central office.⁷⁵ Following the European theory it is said that a company which is organized under the laws of one country and maintains its central office in another is invalid at the situs of its central office because it was not organized in accordance with the laws prevailing there.⁷⁶

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 this essence of the rule has often been misunderstood, especially in the English literature and by German writers too, the policy behind the rule also has not always been appreciated. The most important viewpoint from which to consider the rule is that of a state that does not want an organi-

⁷² RABEL, *op. cit. supra* note 64, at 33-37; BATIFFOL, *TRAITÉ ÉLÉMENTAIRE DE DROIT INTERNATIONAL PRIVÉ* 232, 453 (1955); WOLFF, *DAS INTERNATIONALE PRIVATRECHT DEUTSCHLANDS* 115 (1954); KOLLEWIJN, *op. cit. supra* note 68, at 16.

This view was crystallized in a uniform law in the Hague Treaty of May 11, 1951, signed by the Benelux countries, but which has never come into effect because it was not ratified by the Netherlands. It stated in article 3 of that treaty that: "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 Kollwijn. According to my 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, *Chronique*, *REVUE TRIM. DE DROIT COMM.* 1959.250, commenting on art. 58 of the Treaty of Rome.

⁷³⁻⁷⁴ Omitted.

⁷⁵ RESTATEMENT, *CONFLICT OF LAWS* §§155, 182 ff (1934); RABEL, *op. cit. supra* note 64, at 31.

⁷⁶ WOLFF, *op. cit. supra* note 57, at 115-116.

zation to establish its principal office in its territory and yet derive its existence and legal character from a foreign state. Thus, in the oldest decision 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, was denied recognition as an American legal entity; having failed to fulfill the German requirements for incorporation, it was treated as a German noncorporate association. When a domestic company transfers its domicil to a foreign country, it loses its personality."⁷⁷

In the view of Mr. Deelen, my Dutch collaborator, Professor Rabel's choice of Amsterdam as a hypothetical site was unfortunate. Mr. Deelen cites with approval Kolloewijn's observation with respect to a corporation formed under foreign law but having its actual central office in Holland as follows:

"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."⁷⁸

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.

An investor cannot safely take advantage of this Dutch liberalism, however, unless he is assured of equally tolerant views in the neighboring countries in which the other part of the game would be played. Despite intimations of similar tolerance by occasional writers in other countries,⁷⁹ 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

⁷⁷ 2 RABEL, *op. cit. supra* note 64, at 37-39.

⁷⁸ KOLLEWIJN, *op. cit. supra* note 68, at 16. The result also seems to be precluded 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.

⁷⁹ E.g., BETZKE, *op. cit. supra* note 69.

prohibition against choosing a central office location which is outside the country of the principal business operations.⁸⁰ 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.⁸¹ The "central" office is identified by reference to activities of management and supervision, rather than manufacture and sale.

According to my collaborators, 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 clearance to 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. It 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 between its operational sites, as, for example, in Luxembourg.

⁸⁰ See RIPERT, *op. cit. supra* note 68, at 396; BATTIFOL, *op. cit. supra* note 72, at 232; WOLFF, *op. cit. supra* note 72, at 115; RABEL, *op. cit. supra* note 64, at 40.

⁸¹ But Loussouarn, in *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.

B. *The "Delawares of Europe"*

The views expressed in the preceding paragraphs may surprise many American lawyers, who have been told that Liechtenstein, 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 incorporating a company which will have its central office and principal operations in other countries, they are false both in law and practice. None of these countries is commonly used or could be advantageously used for such purposes for the reasons already given.

A second meaning of such a metaphor might be that the laws of these countries permit great freedom in financial operations, such as, for example, 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, for example, is lower than that of most industrial states.⁸² I do not have complete information on the incorporation fees in these countries, but I understand that incorporators are not drawn to them by cost advantages of this kind.

It is true, however, that certain investors do seek out these countries as places in which to incorporate and manage their companies, in preference to neighboring countries. There are two principal reasons for making such a choice. Sometimes the reason is that one of these countries has been found to be a genuinely efficient place to locate a central office. Switzerland and Luxembourg are both central in a geographical sense, and they both have a long tradition of permitting the free transfer of international balances. It seems doubtful that Liechtenstein would be chosen for operational advantages of this kind.

A second reason for choosing one of these corporate havens is to form a holding company to hold the shares of *operating* companies which have been organized in other countries. The usual functions of such companies are to serve as a reservoir for profits

⁸² For a convenient comparison of organization fees in various states, see P-H CORP. SERV. §§10011-10061.

which a parent company wants to *take out* of the operating subsidiary, but does not want to *put into* its own treasury, because of the taxes or exchange restrictions which would be incurred. Switzerland, Luxembourg, and Liechtenstein have laws and practices which lend themselves to these purposes. Thus it appears that the analogy between Delaware and the European corporate "havens" is not a close one, although it has some validity.

IV. THE EUROPEAN LAWYERS' ROLE IN INCORPORATION

The procedures of incorporation in the countries of the European Common Market are basically similar to 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 managers 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, this article does 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.

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,"⁸³ much less "corporation lawyer."

⁸³ For general observations of the legal professions in Germany, France, and Italy, see BURDICK, *THE BENCH AND BAR OF MANY LANDS* (1939). For France, see Lepaulle, *Law Practice in France*, 50 COLUM. L. REV. 945 (1950); Brown, *The Office of Notary in France*, 2 INT. AND COMP. L.Q. 60 (1953); Tunc, *Modern Developments in Preparation for the Bar in France*, 2 J. LEGAL ED. 71 (1949). For Germany, see Weniger, *The Profession of the Bar in Germany*, 34 ILL. L. REV. 85 (1939). For Italy, see Sereni, *The Legal Profession in Italy*, 63 HARV. L. REV. 1000 (1950).

A. *The Advocate*

The American may, however, ask for a "member of the bar," and be led without hesitation to an "advocate" (*avocat*, *Rechtsanwalt*, *avvocato*, *advocaat*). The advocate is primarily a courtroom lawyer and is often compared to the English barrister.⁸⁴ 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 1954.⁸⁵ Since solo practitioners are not likely to be highly specialized 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.

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) describes *avocats*, *avoués*, *notaires*, and *agents d'affaires* as varieties of "lawyers."

⁸⁴ For instance, by Brown and Tunc, note 83 *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 power belongs to the solicitor in England and to 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 *can* bind his client.

⁸⁵ HAMELIN, *ABRÉGÉ DES RÈGLES DE LA PROFESSION D'AVOCAT*, art. 207 (1954), citing decree of April 10, 1954, art. 49.

B. *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."⁸⁶ We mention the *avoué* only because the identification of French *avocats* with English "barristers" leads so easily to the identification of French *avoués* with English "solicitors."⁸⁷ 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 farther 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 the oral advocacy must be done by the advocate. An American translation for this peculiar intermediary might be "attorney-of-record."

These functions of the "attorney-of-record" resemble some of the functions of an English solicitor. But the "attorney-of-record" performs none of the functions of business counseling, property management, and drafting non-litigious documents, which probably occupy the larger part of an English solicitor's time, and which qualify him to advise an American investor. The latter functions are performed in France chiefly by notaries.⁸⁸

"Attorneys-of-record" form a separate profession only in France, and not even in all districts of that country. Although the function may be recognized in other countries as separate from that of advocacy, the same people usually perform both.⁸⁹

C. *The Notary*

The European notary is also a lawyer.⁹⁰ That is, he is a man who has a university law degree, or who has at least passed profes-

⁸⁶ See ROBSON, *THE ATTORNEY IN 18TH CENTURY ENGLAND* (1959); or, more briefly, Bastian, *The Profession of Law in England and America*, 46 A.B.A.J. 817 (1960).

⁸⁷ They are compared by the distinguished comparatist Tunc, *op. cit. supra* note 83, at 71, note 1. Tunc emphasized that the French *avoué*, like the English solicitor, has the power to "represent" his client.

⁸⁸ Cf. Brown, *supra* note 83, at 60.

⁸⁹ In Italy, a young lawyer is first admitted to practice as an "attorney-of-record" (*procurazione*); after five years he may also become an *avvocato*, and thereafter performs both functions. See Sereni, *The Legal Profession in Italy*, 63 HARV. L. REV. 1000 (1950). Luxembourg lawyers are commonly designated by the double title, *avocat-avoué*.

⁹⁰ See SCHLESINGER, *THE NOTARY AND THE FORMAL CONTRACT IN CIVIL LAW* (1941), New York State, Report of the Law Revision Commission 403 (observations on France, Germany, and Switzerland). See also Brown, *supra* note 83, at 60.

sional 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 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.⁹¹

Urban notaries frequently specialize in corporate practice. It is no accident that some of the best French treatises on company law have been written by the editor of the *Journal des Notaires*.⁹²

D. *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. One Italian advocate has advised us that his accountant competitors are perfectly competent in corporate matters; 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

⁹¹ My Netherlands collaborator, Mr. Deelen, says that in his country the notary invariably drafts any instrument which is required to be notarized.

⁹² Moreau, Editor-in-Chief of the *Journal des Notaires*, is the author of *LES SOCIÉTÉS CIVILES* (1954), *LA SOCIÉTÉ ANONYME* (1948), *LA SOCIÉTÉ A RESPONSABILITÉ LIMITÉE* (1952).

partly as intermediaries for notaries and tax specialists who may be needed.⁹³ The existence of these unlicensed operatives in a semi-legal 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*),⁹⁴ oral argument (by the *avocat*), and drafting of non-litigious documents (by the *notaire*). As an incident of this fractionation, counseling has become nobody's profession. Some of these unlicensed counselors are certainly quite competent, while others certainly are not. Obviously the caution which is used in choosing any adviser should be increased when choosing one who is under no professional regulation or discipline.

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," advocates, and notaries, they may lawfully carry on activities which would be considered the "practice of law" if carried on in the United States.⁹⁵

E. *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;⁹⁶ and they are necessary in France to complete the company organization.⁹⁷ In the formation of limited liability com-

⁹³ See Lepaulle, *supra* note 83, at 947.

⁹⁴ In discussing French procedure in English one must distinguish between the written contentions, technically called "pleadings" in Anglo-American law [See "Pleading," BOUVIER, LAW DICTIONARY], 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.

⁹⁵ An English solicitor and law teacher, Mr. L. Neville Brown, informs us that in England also "the lawyers' monopoly . . . has been eaten away, so far as counseling in tax and corporation matters is concerned, by the professional accountant and various business consultants. . . ."

⁹⁶ *Belgium*: C. Com. I-IX, arts. 29, 31, 33; *Germany*: AktG, §16. The law requires notarial or judicial acknowledgment; notarial is the practical choice. *Luxembourg*: Company Law, arts. 26 and 30; *Netherlands*: W.K., art. 36.

⁹⁷ The cash subscriptions must be originally paid either to the National Deposit Bank (*Caisse de dépôts et consignations*), or to a notary; when the required fraction of subscriptions has been paid in, the proceeds can be released to the company officers only on a notarial affidavit that the conditions have been fulfilled. Law of 1867, art. 1. The simpler and most preferred procedure is to use a notary for both functions.

panies, they are required in Belgium, Germany, and Italy,⁹⁸ 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 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.

This conclusion should be tempered by two warnings. 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 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 needed. Likewise, an American lawyer practicing 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.

V. THE ORGANIC DOCUMENTS

A. *Draw Them in Europe!*

The late Professor Ascarelli once remarked that it is of secondary importance whether the American investor asks an advocate,

⁹⁸ Belgium: C. Com. I-IX, art. 4; Germany: GmbHG, §2; Italy: C. Civ., art. 2475.

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 Milan or Hamburg for "minor modifications." Not only are such articles invariably far from the demands of local law and practice, but they impose on a European lawyer the impossible job of explaining to an American client why they must be changed. What the American client should send to Milan 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 his European adviser.

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

B. *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; the functions of the two American documents are performed by a single European one.

One might equally confuse his European counsel by asking him to draw a set of "articles"; 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." It may be helpful to have at hand some of the European names of the formative documents, *acte constitutif*, *Gründungsvertrag*, *atto costitutivo*, or *akte van oprichting*.

These European names are not, however, the end of the matter. 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 incorporation; 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, including amendments; 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*,⁹⁹ *statuti*, and *statuten*.¹⁰⁰

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.¹⁰¹ In all limited 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.

C. 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."¹⁰²

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. A European lawyer would probably refuse flatly to use anything like it. There are at least two

⁹⁹ *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 and for the partnership limited by shares (*Kommanditgesellschaft auf Aktien*). See, for example, the usage in HUECK, *GESELLSCHAFTSRECHT* 24, 116 (1958).

¹⁰⁰ Several translators have unfortunately translated *statuts*, *statuti*, and *statuten* as "by-laws." This is misleading since these terms are used by Europeans to designate provisions all of which are publicly filed, and some of which are those defining such basic elements as the company's name, purpose, and capital stock.

¹⁰¹ For the principal statutory sections on contents of the articles of incorporation, see the following: *Belgium*: C. Com. 1-IX, art. 30 (*société anonyme*), arts. 120-121 (*société à responsabilité limitée*); *France*: Law of 1867, art. 1 (SA), Law of 1925, art. 14 (SARL); *Germany*: AktG, §16, GmbHG, §3; *Italy*: C. Civ., art. 2328 (SpA), art. 2475 (SARL); *Luxembourg*: Company Law, art 27 (SA), art. 184 (SARL); *Netherlands*: W.K., arts. 36b, 36c, 36d.

¹⁰² LEMEUNIER, *POURQUOI ET COMMENT CONSTITUER UNE SOCIÉTÉ ANONYME*, I-7 (1958).

reasons. One is that the European laws authorize the articles to state *purposes*, not *powers*. The other reason is that the ultra vires doctrine, whose ravages brought forth the inflated American purpose clauses, is little known in Europe.

Broad purpose clauses are apparently tolerated also in Germany, Italy, and Luxembourg, so long as some real purpose exists.¹⁰³ In two nations, Belgium and the Netherlands, vague or omnibus purpose clauses are inadmissible. The Belgian company law was amended in 1958 to require a "precise designation of the purpose of the enterprise."¹⁰⁴ 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.

D. *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 to be held, how they are to be called, who may be admitted, how the agenda is to be determined, how minutes should be kept, and how votes are to be counted. Many of these provisions will be found to restate propositions contained in the company law of the particular country. These portions of the articles are, of course, much like the typical by-laws of an American corporation.

It is obviously inconvenient to be required 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.¹⁰⁵ In Belgium the extract procedure

¹⁰³ My German collaborator, Professor Serick, warns that a company might be successfully attacked if it were formed without any specific purpose in mind, but merely to serve some later need which might appear; that is, a *Gesellschaft auf Vorrat*.

¹⁰⁴ C. Com. I-IX, art. 30 (1), as amended by Law of January 6, 1958.

¹⁰⁵ *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

is used for limited liability companies,¹⁰⁶ but not, unfortunately, for stock companies.¹⁰⁷ Italy, Luxembourg, and the Netherlands require publication of complete articles in all cases.¹⁰⁸

VI. 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,¹⁰⁹ and five in Germany.¹¹⁰ In Italy and the Netherlands, two will suffice for a stock company,¹¹¹ and two will do for a limited liability company in all the countries where such a company may be formed.¹¹² But no member of the Common Market has followed the example of a few American states, which permit a single investor to incorporate.¹¹³

Requirements of this sort give little difficulty to an American lawyer on his home grounds; any group of clerks will do for incor-

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, 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, see HGB, §10.

¹⁰⁶ C. Com. I-IX, art. 7 (b). The Belgian publication requirement includes two items which would probably be found in American by-laws — the fiscal year, and the date of the annual shareholders' meeting.

¹⁰⁷ C. Com. I-IX, art. 9.

¹⁰⁸ *Luxembourg:* Company Law, art. 8; *Netherlands:* W.K., art. 36f. The Italian company laws purport to require only filing in the Commercial Register.

¹⁰⁹ *Belgium:* C. Com. I-IX, art. 29; *France:* Law of 1867, art. 23; *Luxembourg:* Company Law, art. 26.

¹¹⁰ AktG, §2.

¹¹¹ *Italy:* C. Civ., art. 2247. *Netherlands:* No statutory provision requires more than one member; all sections speak of the members in plural terms, and Dutch legal theory regards incorporation as a group action (my Dutch collaborator uses the German term *Gesamtakt*) which requires more than one participant.

¹¹² *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.

¹¹³ IOWA CODE §491.2 (1958); KY. REV. STAT. §271.025 (Baldwin's, 1955); MICH. COMP. LAWS §450.3 (1948).

porators, and shares can be subscribed and paid for in their names. But many European lawyers will object to this kind of practice. My Belgian, French, and Dutch collaborators all warn against unpleasant legal consequences which might result from procedures of this sort; only the German colleague sees no problem. My Luxembourg collaborator, while disapproving the use of straw incorporators, reports that they are 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.¹¹⁴ My Belgian collaborator warns that the straw man commits a crime by falsely representing himself to be a subscriber, which he is not;¹¹⁵ 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 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.¹¹⁶ 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 nonprofit organizations, appears in the Civil Code as a subdivision of the law of contract; the French Civil

¹¹⁴ *Belgium*: C. Com., art. 35.

¹¹⁵ To the same effect, see VAN RYN, *PRINCIPES DE DROIT COMMERCIAL*, Part I, 496 (1954).

¹¹⁶ For a comparison of contractual and institutional concepts, see 1 HAMEL AND LAGARDE, *TRAITÉ DE DROIT COMMERCIAL* 468-9 (1954).

Code's first words on company law are, "An association is a contract. . . ."¹¹⁷

For these and other reasons, European theorists are accustomed to say that a company in which there was only one bona fide investor at the 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.¹¹⁸ In France, heirs were allowed to claim the property of a bank incorporated by their ancestor in league with straw co-investors.¹¹⁹ In Italy, a statute which makes a sole shareholder liable for the company debts might be applied to one who holds some of the shares through straw men.¹²⁰

The burden of procuring incorporators who meet European standards will probably not prove very heavy. For ordinary incorporations, there is no requirement that the incorporators be Europeans;¹²¹ 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 for the incorporators of a Belgian limited liability company and for one of the seven in a French stock company; with these exceptions, they may 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

¹¹⁷ 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."

¹¹⁸ Decision of the Hoge Raad of Nov. 30, 1927, 3067 WEEKBLAD VOR PRIVAATRECHT, NOTARIS-AMBT EN REGISTRATIE (hereinafter W.P.N.R.) 645 (1928); Decision of Jan. 12, 1927, 3023 W.P.N.R. 850; Decision of May 30, 1928, BESLISSINGEN IN BELASTING ZAKEN (hereinafter B.) 4279; Decision of April 15, 1931, B. 4965.

¹¹⁹ Court of Cassation, decision of May 19, 1926, DALLOZ, RECUEIL PÉRIODIQUE ET CRITIQUE, Part I, 25 (1929).

¹²⁰ C. Civ., art. 2362. Mr. Bruna, one of my Italian collaborators, states that prevailing Italian opinion permits holding through strawmen, unless there be a subjective intent to escape obligations.

¹²¹ There are very few exceptions, such as, in France, petroleum extraction companies and newspaper publishing companies.

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 my French informants, who is most positive about the danger of straw men, assures me 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 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.¹²²

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

VII. CAPITAL AND ITS PAYMENT

A. *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 percent subscribed. Some of the statutes say expressly that the company is not perfected until it reaches this point;¹²³ even when the statutes are silent, the law is probably the

¹²² Decision of the Hoge Raad of Dec. 14, 1932, B. 5339.

¹²³ *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*: C. Civ., art. 2329 (1) (stock companies); *Luxembourg*: Company Law, art. 26 (stock companies), art. 183 (limited liability companies).

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 means simpler than obtaining a shareholders' vote on a charter amendment. Italy and Germany permit stock companies to adopt charter clauses which authorize the managers to increase the capital.¹²⁴ 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." France also has some statutory provisions permitting "variable capital,"¹²⁵ but they are somewhat inconvenient, and are little used.¹²⁶ 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 percent in Belgium and Luxembourg, 25 percent in France and Germany, and 30 percent in Italy.¹²⁷ The limited liability company laws in France and Luxembourg require payment of 100 percent of the amount subscribed,¹²⁸ but elsewhere the same fractional payments as in stock companies are permitted.¹²⁹

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,¹³⁰ and the Belgian law is the same.¹³¹ Elsewhere, the

¹²⁴ *Germany*: AktG, §169; the increase is limited to 50% of the stock before the increase. *Italy*: C. Civ., art. 2443.

¹²⁵ Law of 1867, arts. 48-52.

¹²⁶ 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 shares, or be expelled (art. 52).

¹²⁷ *Belgium*: C. Com. I-IX, art. 32; *France*: Laws of 1867, art. 1, ¶2. The balance must be paid within five years. Law of March 4, 1943, art. 1. *Germany*: AktG, §28 (2); *Italy*: C. Civ., art. 2329; *Luxembourg*: Company Law, art. 26.

¹²⁸ *France*: Law of 1925, art. 7; *Luxembourg*: Company Law, art. 183.

¹²⁹ *Belgium*: C. Com. I-IX, art. 120. However, at least 50,000 francs (about \$1,000) must be paid in, whatever fraction of the whole it may be. *Germany*: GmbHG, §7; *Italy*: C. Civ., art. 2476 (cross-referring to stock company requirements).

¹³⁰ Law of 1867, art. 4.

¹³¹ As to limited liability companies, full payment of property contributions is expressly required by C. Com. I-IX, art. 120. As to stock companies, the requirement of full payment

rules for payments in property are no stricter than for payment in money, and perhaps less so.¹³²

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.

By stating the matter in this way, I am greatly oversimplifying the theory. In theory, it is possible to have an incorporation "by stages,"¹³³ 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 percent of the offered shares; in that event, the incorporation would collapse. 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. However, it may well be used in a later *increase* of capital.

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.¹³⁴ Of the fifth subscribed, only one-tenth needs to be paid on each subscribed share;¹³⁵ a company could properly carry

rests on the opinions of commentators. See VAN RYN and HEENEN, 2 DROIT COMMERCIAL 11 (1957).

¹³² See GODIN-WILHELM, AKTIENGESETZ §28, note 11 (1950).

¹³³ Known to French commentators as *fondation successive*, and to Germans as *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.

¹³⁴ Netherlands: W.K., art. 36e. The subscriptions are a prerequisite to issuance of the Certificate of Incorporation, without which companies are forbidden to do business.

¹³⁵ 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.

on business with as 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 \$5,000 for a limited liability company.¹³⁶

B. 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, Anteil, 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 an *Anteil* 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

¹³⁶ *Belgium*: No minimum for a stock company; BFr 50,000 (about \$1,000) for SPRL. 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 \$1,500) for a stock company, C. Civ., art. 2327 [reportedly due to be increased to 25,000,000 IL (about \$40,000)]. 50,000 IL (about \$75) for SARL, C. Civ., art. 2474 [reportedly due to be increased to 1,500,000 IL (about \$2,500)].

Luxembourg: No minimum for stock company. 100,000 Lfr. (about \$2,000) for SARL. Company Law, art. 182.

Netherlands: No minimum.

an undivided fraction of the equity, as in an American partnership. He buys 200 out of 1,000 shares, not merely a "20 percent interest."

The shares have stated money values, such as 500 francs or 100 marks,¹³⁷ except that Belgium and Luxembourg permit stock companies to issue shares without par value.¹³⁸ The other countries do not authorize no-par shares.

In Europe, as in America, it is forbidden to issue shares for less than par,¹³⁹ but there is no law against issuing them above par, perhaps ten or twenty times above par.¹⁴⁰ Since the European minimum par values are fairly low (about \$1.50 for limited liability company shares in Italy, about \$10 in France),¹⁴¹ it would be theoretically possible to introduce the "low-par" system in vogue in the United States. However, no one has done so, and it would not necessarily result (as it does in Delaware) in creating a large "surplus" which would be free of the restrictions placed on capital.¹⁴²

C. *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 paid nothing, or for which they paid in property taken at gross overvaluations, with disastrous results for innocent investors and creditors.

To these evils American courts responded with doctrines making subscribers liable for any deficiency in the value of consideration received for their shares.¹⁴³ Later, legislatures reacted with

¹³⁷ There are minimum share values in some countries: *France*: 5,000 Ffr (about \$10) for SARL, Law of 1925, art. 6; *Germany*: 100 DM (about \$25) for AG, AktG, §8; 500 DM (about \$125) for GmbH, GmbHG, §5; *Italy*: 1,000 IL (about \$1.50) for SARL, C. Civ., art. 2474; *Luxembourg*: 500 Lfr (about \$10) for SARL, Company Law, art. 182.

¹³⁸ *Belgium*: C. Com. I-IX, art. 41; *Luxembourg*: Company Law, art. 37.

¹³⁹ In the Netherlands, the underwriter may receive a discount of 6%. W.K., art. 38a.

¹⁴⁰ Liberty to sell for more than par is specifically granted in German stock companies. See AktG, §9 (2).

¹⁴¹ See note 137 *supra*.

¹⁴² German stock company law requires that any premium over par value be stated in the publicly-filed documents of organization, and that the premium should form part of a legal reserve which is not available for dividends. AktG, §§16 (2), 28 (2); §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, but apparently permits disbursement after that time. C. Civ., art. 2430.

¹⁴³ *Scovill v. Thayer*, 105 U.S. 143 (1881); STEVENS, HANDBOOK ON THE LAW OF PRIVATE CORPORATIONS §183 (1949); BALLANTINE, CORPORATIONS §§343 et seq. (1947).

Blue Sky laws, designed to enable government officials to determine whether the initial investments in the company had been duly made.¹⁴⁴ 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.¹⁴⁵ 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, such payments do not have to be banked, but if they are, the bank must certify that the deposits are unrestricted.¹⁴⁶

For the payment of subscriptions in property, the special regulations are more numerous and more complicated. One requirement is that payments in property must be 100 percent paid in before the company is fully incorporated; in France and Belgium, the payments on account which are sometimes permissible for cash subscriptions are inadmissible for subscriptions payable in property.¹⁴⁷

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.¹⁴⁸ It is the rule for limited liability companies in France,¹⁴⁹ and for stock companies in the Netherlands.¹⁵⁰

¹⁴⁴ LOSS AND COWETT, BLUE SKY LAW 1-10 (1958); LOSS, SECURITIES REGULATION 7-16 (1951).

¹⁴⁵ France: Law of 1867, art. 1. The funds must be deposited in the official national depository — *Caisse des Dépôts et Consignations* — or with a notary. Italy: C. Civ., art. 2329. The payments must be made to a special account in any bank.

¹⁴⁶ AktG, §§28 (2), 29 (1).

¹⁴⁷ See notes 130, 131 *supra*.

¹⁴⁸ Belgium: C. Com. I-IX, art. 30 (stock company), art. 121 (limited liability company); Germany: AktG, §20; GmbHG, §5 (4); Luxembourg: Company Law, art. 27 (stock company), art. 184 (limited liability company).

¹⁴⁹ Law of 1925, art. 8.

¹⁵⁰ W.K., art. 40a. Netherlands, of course, has no limited liability companies.

A third regulation sometimes encountered is a requirement of appraisal; the most complicated plan of this nature is found in the French stock company law.¹⁵¹ 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 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.¹⁵² 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.¹⁵³

A fourth precaution taken by some legislators has been to impede transfer of the shares received for property. In French stock companies, shares issued for property cannot be represented by certificates, and are non-negotiable, for two years after incorporation;¹⁵⁴ in Belgium, they are not freely negotiable for approximately two years;¹⁵⁵ in Italy, they are non-transferable until the directors and auditors have made the post-incorporation appraisal.¹⁵⁶

A fifth hazard is reserved for the property-subscribers in a French limited liability company.¹⁵⁷ Instead of having an appraisal 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.

¹⁵¹ Law of 1867, art. 4.

¹⁵² AktG, §§25, 26, 34.

¹⁵³ C. Civ., art. 2343 (stock companies), art. 2476 (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 the deficiency in money. The subscriber may elect to withdraw entirely, resulting in a still greater reduction in stated capital.

¹⁵⁴ Law of 1867, art. 3 (5).

¹⁵⁵ 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.

¹⁵⁶ C. Civ., art. 2343; the code declares the shares inalienable (*inalienabili*) during this period.

¹⁵⁷ Law of 1925, art. 8.

These various regulations are not only burdensome; they are also rather fearsome beartraps, since any failure to comply may result in "invalidity" of the corporation, or liability of the incorporators, or both. The French legislator, in particular, seems to have prepared ambushes 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 operations in the area, the parent will be expecting to contribute both money and the property which was used in the pre-incorporation business. 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 to avoid 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 managers; 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,¹⁵⁸ or made within two years thereafter.¹⁵⁹

VIII. FILING AND APPROVAL

The procedures of incorporation do not usually involve long waits for administrative action. In all the Common Market coun-

¹⁵⁸ AktG, §20. See also §45, concerning purchases of property amounting to one-tenth of the corporate capital.

¹⁵⁹ AktG, §45.

tries 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, and the papers deposited, there is nothing to wait for.

Even for foreigners, there are no administrative waits in connection with ordinary incorporation.¹⁶⁰ 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 obtaining licenses to be merchants or corporate executives; in obtaining licenses to exchange money for the purpose of investment; or in obtaining 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 various factors — whether the new industry will further complicate an oversupply 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.

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

¹⁶⁰ The principal exceptions are (1) specially regulated types of enterprises, such as banks and insurance companies, and (2) enterprises in which foreign participation is limited, such as (in France) petroleum extraction and newspaper publication.

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 *dirretore*. 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 from those which he knows.

Most 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 re-creating 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 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.