Erika Kovács | Martin Winner

Stakeholder Protection in Restructuring

Selected Company and Labour Law Issues

Nomos

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Foreword

Corporate restructurings such as national and cross-border mergers and divisions, as well as cross-border conversions, enable companies to grow and adapt to a changing environment. At the same time, they can have a significant impact on companies' stakeholders, in particular creditors, shareholders, and employees. Corporate restructurings entail even additional risks for these groups if they occur across borders.

The current regulation of cross-border corporate mobility within the European Union provides a very fragmented picture and consists of a mixture of harmonized EU regulation, case law of the Court of Justice of the EU, and national rules. In the development of the Common Market, it is crucial for the EU to facilitate freedom of establishment. The Commission's proposal on corporate cross-border mobility from April 2018[1] intends to foster the cross-border mobility of companies between the Member States by the creation of a predictable and harmonised legal framework across the EU. The contributions were drafted in 2018 and partly updated in February 2019. Developments since that time could not be taken into account.

The contributions in this book address the challenges company law and labour law face in both national and cross-border corporate restructurings. Both the company and the labour law angles are crucial for an adequate treatment of the topic as, in the face of the ever-growing internationalisation of the corporate world, our legal systems have to pursue some delicate balances – on the one hand, between flexibility and security and, on the other hand, between the conflicting aims of economic growth and employment protection.

This collection contains the results of a conference we organised on 12-13 February, 2018, at the Vienna University of Economics and Business with the title 'Stakeholder Protection in Restructuring – Selected Company and Labour Law Issues', where company and labour lawyers discussed the implications and pitfalls of corporate reorganisations and the possible legal answers. The conference was the closing event of the IMPULSE project, in which company and labour lawyers from the Vienna University

1 Proposal of the European Commission for a Directive amending Directive (EU) 2017/1132 as regards cross-border conversions, mergers and divisions.

of Economics and Business, Austria, the Faculty of Law of the University of Belgrade, Serbia, and the Ss. Cyril und Methodius University, Macedonia, cooperated and conducted a comprehensive research on restructuring of companies from the perspective of the EU requirements. The cooperation was financed by the Austrian Agency for International Cooperation in Education and Research (OeAD, Österreichischer Austauschdienst) for the term 1st April 2016 – 31st March 2018.

The book includes four essays on company law challenges. Fuentes analyses the European legal framework regarding cross-border conversions, while Winner covers creditor protection in domestic and cross-border mergers in European law. Mirjana Radović and Vuk Radović focus on creditor and shareholder protection in various forms of restructurings in Serbian law. The six papers on labour law address two major issues related to company restructuring, namely transfers of undertakings and employee participation in the boards. The cross-border corporate restructuring of the company creates a challenge for employee participation in the boards. The contributions of Seifert and Kovács provide a critical analysis of the existing and planned European legal framework on this issue. Ales reveals the controversial issues of the Transfer of Undertakings Directive, while Niksova deals with the cross-border transfer of undertakings. Finally, the papers of Kovačević and Kalamatiev/Ristovski highlight the national pitfalls of the implementation of the European rules on transfer of undertakings.

We do hope you will enjoy reading the contributions.

Vienna, March 2019 Erika Kovács and Martin Winner

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Authors

Edoardo Ales is a senior, level I expert in EU, comparative, foreign and national Labour and Social Security Law as well as in EU Employment and Social Inclusion policies. He has teaching and research experiences all around Europe. He has coordinated, participated and evaluated various EU and national level research projects for the EU Commission, for the European Parliament and for national research authorities. Since 2006, he is member of the Scientific Committee and National Expert for Italy of the European Labour Law Network (ELLN now ECE). He his author of various book and articles as well as member of boards of directors of international journals. He has been keynote speaker at many international conferences and he has organized several of them. As co-editor he has recently published with Y. Curzi, T. Fabbri, O. Rymkevich, I. Senatori, G. Solinas, *Working in Digital and Smart Organizations. Legal, Economic and Organizational Perspectives on the Digitalization of Labour Relations*, London – New York – Shanghai: Palgrave Mcmillan, 2018 and with M. Bell, O. Deinert, S. Robin-Olivier, *International and European Labour Law. A Commentary*, Baden – Baden: Nomos Verlag, 2018.

Todor Kalamatiev is Full Professor and Head of the Department of Labour and Social security law at the 'Ss. Cyril and Methodius' University in Skopje (Faculty of Law 'Iustinianus Primus' - Skopje). From 2008 to 2012, Professor Kalamatiev was a Vice Dean for Education at the Faculty of Law 'Iustinianus Primus' – Skopje. He teaches labour law and other similar subjects at the undergraduate, postgraduate and doctoral studies within the Faculty of Law 'Iustinianus Primus'. Professor Kalamatiev also is a Member of the Study Group on a Restatement of Labour Law in Europe and a National Expert for the Republic of Macedonia in the European Labour Law Network.

Ljubinka Kovačević, Dr. iur., is Associate Professor at the University of Belgrade Faculty of Law in Serbia. Prior to joining this Faculty in 2005, she was a researcher at the Institute of Comparative Law in Belgrade. She is the author of two monographs ("Legal subordination in employment relationship and its limitations" /2013/ and "Valid reasons for dismissal" /2016/) and many papers on Serbian, international, European and comparative labour law and social security law.

Erika Kovács, Dr. iur., is Assistant Professor at the Vienna University of Economics and Business (WU) in Austria. She read law in Hungary and Germany and worked for the IAAEU at the University of Trier, where she completed her doctoral thesis. Prior to joining the WU in 2012, she was a researcher at the University of Pécs, Hungary. She is specialized in European and Austrian labour and social security law.

Mónica Fuentes Naharro, Dr. Iur., is (tenured) Associate Professor at the Law Faculty of the Universidad Complutense de Madrid, in Spain. She is also of Counsel at Estudio Jurídico Sánchez Calero. She lectures business law (company law, financial markets, contracts and insolvency law), and is specialized in company law. She is a member of several international company law groups' experts: the EMCA (European Model Company Act), the ICLEG (Informal Company Law Experts Group) and the European Business Code.

Diana Niksova, Dr. iur., is a 'post-doc' Research and Teaching Associate at the Department of Labour Law and Social Security Law at the University of Vienna. Her main research interests lie in the field of Austrian and European labour and social security law, with a strong focus on cross-border situations. Currently (in 2018/19), she is an academic visitor at the Institute of European and Comparative Law (IECL) at the University of Oxford.

Mirjana Radović, Dr. iur., LL.M. (Humboldt), is an Associate Professor at the Faculty of Law University of Belgrade. After obtaining her magister degree at the Faculty of Law in Belgrade (in 2006), she finished her LL.M. studies at the Faculty of Law, Humboldt University in Berlin (Germany), where her master's thesis "*Möglichkeiten und Grenzen des Depotstimmrechts*" was awarded as the best master's thesis in 2006/2007. She obtained her PhD at the Belgrade Faculty of Law in 2011. Mirjana Radović specialises in Capital Markets Law, Company Law, Commercial Law, Banking Law and Law on Electronic Communications. Her most important monographs include: 1. *The Law on Payment Services* (2016); 2. *Safeguarding and Administering Securities* (2014); and 3. *Contract on Interconnection of Public Telecommunication Networks* (2008).

Vuk Radović, Dr. iur., is a Full-time Professor at the Faculty of Law University of Belgrade, where he is currently teaching the following courses: Company law, Commercial law, Bankruptcy law and EC Company law. Apart from the Faculty of Law in Belgrade, he has been teaching courses at other faculties as well, such as the Faculty of Law in Graz, the Faculty of Geography in Belgrade, the Faculty of Law in East Sarajevo and the Faculty of Law (UDG) in Podgorica. Most important books: 1. *Bankruptcy Law – Part I (introduction to bankruptcy law, basic notions of bankruptcy law, bankruptcy proceeding, legal consequences of opening bankruptcy proceeding)*, 2018, 2. *Bankruptcy Law – Part II (avoidance powers, reorganization, international bankruptcy, bankruptcy of corporate groups)*, 2018, 3. *Company Law of the EU*, 2011, 4. *Executive Compensation*, 2011, 5. *Target Company Defensive Tactics Against Takeovers*, 2008.

Aleksandar Ristovski is Assistant Professor at the 'Ss. Cyril and Methodius' University in Skopje (Faculty of Law 'Iustinianus Primus'). He teaches labour law and other similar subjects at the undergraduate and postgraduate studies within the Faculty of Law 'Iustinianus Primus' – Skopje. Dr. Ristovski is a Member of the Study Group on a Restatement of Labour Law in Europe and a National Expert for the Republic of Macedonia in the European Labour Law Network. He also is a member of the CEElex network of national legal experts on labour and industrial relations in Central and Eastern Europe.

Achim Seifert is Professor in Private Law, German and European Labour Law and Comparative Law at the Friedrich-Schiller-University Jena/Germany. He previously taught European and International Labour Law at the University of Luxembourg. His main fields of interest are European and International Labour Law as well as Comparative Labour Law, Employee Participation, the Horizontal Effect of Fundamental Rights and Employee Data Protection. Achim Seifert serves as Member of the Editorial Board of the European Labour Law Journal (ELLJ), the Comparative Labor Law & Policy Journal (CLLPJ) and of the Revue de droit comparé du travail et de la sécurité sociale.

Martin Winner, Dr. iur. and Mag. rer. soc. oec., is full professor of business law at the Vienna University of Economics and Business (WU) in Austria. He is also Chairman of the Austrian Takeover Commission, the regulator for public takeovers in Austria. As member of the Informal Expert Group on Company Law (ICLEG), he has advised the European Commission *inter alia* in the course of the preparation of the recent corporate mobility package. Martin Winner areas of experise lie in company law, capital markets law, intellectual property law and comparative law with a special focus on CEE.

Cross-Border Conversions and the Company Law Package

Mónica Fuentes Naharro[*]

Summary

A. The Need for a European Legal Framework Regarding Cross-Border Conversions

By means of a cross-border transfer of seat, a legal entity governed by the Member State of origin is converted into a legal entity governed by the law of the chosen Member State, retaining its legal identity but changing its *lex societatis.* Hence, it is correct to say that the company is converted (or "reincorporated") into another one: the legal type chosen at the new Member State.

Currently, the term "conversion" has replaced that of the "transfer of seat" traditionally used by scientific doctrine and by the Draft Fourteenth Directive, which is associated, as widely known, with the problem of defining what "seat" means as a connecting factor and the policy issues associat-

* Associate Professor at the Law Faculty of the Universidad Complutense de Madrid.

ed with it ("incorporation theory" *versus* "real seat theory"). Besides, the fairly widespread use of the term "conversion" reveals a policy approach focused — more correctly — on the legal nature of the transaction (that of a "structural change").[1]

I. Lack of Legal European Harmonization and Difficulties of Converting Cross-Border

The "right to convert cross-border" is protected by European primary law under the principle of freedom of establishment (Arts. 49 and 54 of the Treaty — TFEU) and by the European Court of Justice (ECJ) jurisprudence (*Sevic*,[2] *Cartesio*,[3] *Vale*[4] and, more recently, *Polbud*).[5] However, there is no secondary law in the European Union ("EU") for implementing cross-border conversions. In regards to cross-border mobility, the European law provides a specific legal framework only for (1) cross-border mergers through the Directive 2005/56/CE (current Chapter 2 of the consolidated company law Directive 2017/1132);[6] and (2) for the cross-border transfer of seat of the *Societas Europaea* (SE) (Art. 8 SE Regulation)[7] and the *Societas Cooperativa Europaea* (SCE) (Art. 7 SCE Regulation).[8] Thus, there is no harmonization on this issue at the European level.

Although the absence of rules in European secondary law is not a precondition for the implementation of the freedom of establishment, it is likely to deter companies that have their seat in another Member State from exercising the freedom of establishment laid down by the Treaty; thus, a harmonization of European law would be desirable to facilitate

1 Many national laws consider that this transaction has a legal nature relating to the structural change of a company, as in the case of Spanish law: see Art. 92 et seq. of Ley 3/2009 on *Modificaciones Estructurales* (hereafter, "LME").
2 C-411/03 *Sevic*, EU:C:2005:762.
3 Case C-210/06 *Cartesio*, EU:C:2008:723.
4 C-378/10 *VALE*, EU:C:2012:440.
5 C-106/16 *Polbud*, EU:C:2017:80.
6 Directive 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law (codification) [2017] OJ L 169/46.
7 Council Regulation (EC) No. 2157/2001 of 8 October 2001 on the Statute for a European Company.
8 Council Regulation (EC) No. 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society.

cross-border conversions.[9] The lack of harmonization leads to several problems. Some Member States do provide a legal framework (or permit these operations through the analogous application of the cross-border merger rules or SE rules), but the differences and inconsistencies among them – among those different legal frameworks- make cross-border conversions much more difficult to carry out and, in any case, increase legal advisory costs due to the technical difficulties associated with them. Some other Member States do not provide any legal framework at all (neither accepting the analogical application of cross-border merger rules or SE rules) and require a prior liquidation and subsequent reincorporation.

Recently published studies on the initiative of both the European Commission and Parliament, the *Study on the Law Applicable to Companies* (2016)[10] and the *Cross-Border Mergers and Divisions, Transfers of Seat: Is There A Need to Legislate*? (2016),[11] respectively, as well as the Commision's *Inception Impact Assessment*, have supported the need to adopt a cross-border conversion directive on these same grounds.[12]

II. The Company Law Package

The problem already outlined is currently in the spotlight. However, it is not a new problem. The project of a directive on cross-border transfer of seat has been on and off the European Commission's agenda for the past 20 years, ever since a first pre-proposal in 1997,[13] and again when it was

9 Case C-378/10 Vale Építési kft, paras 36-38. Carsten Gerner-Beuerle, Federico M. Mucciarelli, Edmund-Philipp Schuster, Mathias Siems, "Cross-Border Reincorporations in the European Union: The Case for Comprehensive Harmonization", *Journal of Corporate Law Studies*, vol. 18, 1 (2018), 1-42; Vanessa Knapp, "Cross-Border Mobility: What Do We Need in Practice?", *ERA Forum* (https://link.springer.com/article/10.1007/s12027-018-0495-6) (2018).

10 https://publications.europa.eu/en/publication-detail/-/publication/259a1dae-1a8c-11e7-808e-01aa75ed71a1/language-en.

11 http://www.europarl.europa.eu/thinktank/en/document.html?reference=IPOL_STU(2016)556960.

12 Final Report (2017) *Inception Impact Assessment* https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017-2377472_en.

13 Proposal for a Fourteenth European Parliament and Council Directive on the transfer of the registered office of a company from one Member State to another with a change of applicable law, YV/D2/6002/97-EN REV. 2.

"revived" in the 2012 Action Plan.[14] Within the context of this Action Plan, the Commission launched a call for experts in company law to provide ideas and technical support on cross-border mobility in general (i.e., to regulate cross-border conversions, improve directives on cross-border mergers and, in certain cases, to regulate cross-border divisions), as well as to develop a study on the recognition of the so-called "interest of the group" and the transparency of the corporate group's structure. This group of experts is known as the Informal Company Law Expert Group (ICLEG) and has worked for the European Commission since 2014,[15] discussing how to improve cross-border transactions of EU companies, as it may be inferred from the minutes of the group's meetings.[16]

The collaboration of the ICLEG with the European Commission has led to the drafting and recent publication by the Commission of the so-called Company Law Package, on April 25th of this year (2018).[17] This package aims at establishing "*simpler and less burdensome rules for companies*" regarding incorporations and cross-border transactions and consists of two Proposals.

The Commission's Proposal 2018/0114[18] on cross-border mobility addresses cross-border conversions, mergers and divisions by amending and incorporating several provisions into the current (codified) company law Directive 2017/1132. As already known, this directive already includes rules for internal mergers, divisions and cross-border mergers. The proposal introduces some changes in the existing regulation of cross-border mergers. However, the most novel addition is the introduction of common procedures for cross-border divisions and conversions. These procedures closely follow the existing one for cross-border mergers, in particular the drawing

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14 The Commission, in its Action Plan on European Company law and corporate governance – a modern legal framework for more engaged shareholders and sustainable companies, of 12 December 2012, COM(2012) 740 final, announced that it would continue to study the need and viability of a directive on the cross-border transfer of company seats.

15 Its members are: John Armour, Gintautas Bartakus, Blanaid Clarke, Pierre-Henri Conac, Harm-Jam de Kluiver, Holger Fleischer, Mónica Fuentes, Jesper L. Hansen, Vanessa Knapp, Marco Lamandini, Arkadiusz Radwan, Christoph Teichmann, Robbert van Het Kaar, Martin Winner: http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetail&groupID=3036.

16 http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetail&groupID=303.

17 https://ec.europa.eu/info/publications/company-law-package_en.

18 https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=COM:2018:241:FIN&from=EN.

up of the draft terms and the director's and expert's reports, disclosure of these documents, shareholders' approval, and finally, assessment and issuance of a certificate by the competent authority of the Member State of origin (or home MS) and registration in the Member State of destination (or host MS).

The Commission's Proposal 2018/0113 intends to promote the use of digital tools and procedures in company law.[19] Member States will need to allow a fully online procedure for the registration of new companies and branches of other companies, permitting incorporation without the physical presence of any member before any public authority (except when a fraud or abuse might concur). Proposal 2018/0113 "*sets safeguards against fraud and abuse such as mandatory identification control, rules on disqualified directors and a possibility for Member States to require the involvement of a person or body in the process, such as notaries or lawyers*". The proposal also establishes the need to offer free access to companies' most relevant information in the registers. This Proposal will require important changes in national legislation and its implementation will be a technological challenge for the Member States that want to preserve the current level of control in the incorporation of companies. The question of online identification will undoubtedly be of special interest and complexity, especially in countries (such as Spain) that use a Latin notarial system (or Roman system).

Though the Proposal on digitalization certainly deserves more detailed examination, this paper is focused on Proposal 2018/0114 regarding cross-border conversions, mergers and divisions (hereinafter also referred as "Cross-border Mobility Proposal" or just "Proposal"), and, more specifically, on the cross-border conversions regime and the main policy issues addressed by it, especially regarding the protection of stakeholders. To that end, we will refer to (1) the technical work and debates within the ICLEG — as to the extent, only, of the contents published in the minutes;[20] (2) the several studies published on this specific issue (mainly, the 2016 studies drawn up at the request of the Commission and Parliament on cross-border transfer of seat and applicable law to companies); and (3) those solutions contained in other European legal instruments (mainly, current cross-border mergers and European Company rules) and compared law (mainly, Spanish law).

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19 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM%3A2018%3A239%3AFIN.

20 https://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetail&groupID=3036.

B. The Cross-Border Mobility Proposal. Main Policy Issues on Cross-Border Conversions

I. Scope of the Proposal

One of the first policy issues to be addressed when facing the regulation of cross-border conversions was on whether the subjective scope should be extended to include all forms of establishments (as envisioned in Art. 54 TFEU),[21] to all limited liability companies (public and private), or to public limited liability companies only.[22]

The Proposal has opted for a restricted subjective scope around all limited liability companies listed in Annex II of the Directive 2017/1132 [Art. 86.a)1º], giving Member States the ability to exclude cooperatives and collective investment entities [Art. 86.a) 3º, 4º]. Besides this, the Proposal has excluded the possibility to convert for companies in situations such as winding up, liquidation or a severe financial crisis[23] [Art. 86.c) 2º] as well as to those conversions implying an abuse of law [Art. 86.c) 3º] under the wide concept of "*artificial arrangement aimed at obtaining undue tax advantages or at unduly prejudicing the legal or contractual rights of employees, creditors or minority members*" (see *infra* B.II and III).

II. The Real Seat Theory Issue: To Set Aside?

1. The Controversial

The most delicate policy issue on cross-border conversions refers to the selection of the connecting factor for the *lex societatis* to be applied: either a

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21 *Cross-Border Mergers and Divisions, Transfers of Seat: Is There A Need to Legislate*? (2016) (9, 33); see the debates in the ICLEG Minutes from July 10th and 11th, 2017.

22 See the debates in the ICLEG Minutes from May 15th, 2017.

23 Art. 86.c establishes: "A company shall not be entitled to carry out a cross-border conversion in any of the following circumstances: (a) proceedings have been instituted for the winding up, liquidation, or insolvency of that company; (b) the company is subject to preventive restructuring proceedings initiated because of the likelihood of insolvency; (c) the suspension of payments is on-going; (d) the company is subject to resolution tools, powers and mechanisms provided for in Title IV of Directive 2014/59/EU of the European Parliament and of the Council; (e) preventive measures have been taken by the national authorities to avoid the initiation of proceedings referred to in points (a), (b) or (d)."

formal one like the registered office, as in the case of those countries aligned with the so-called "incorporation theory", or a material one (head office or central administration), as with those countries following the so-called "real seat theory". The question of whether or not to impose the real seat theory through secondary law (and then require that the central administration or head office move together with the registered office), has turned out to be a type of "classic" controversy whenever any cross-border operation related to the freedom of establishment enters into discussion. In fact, this issue "obstructed" and, finally, prevented a clear move forward with the adoption of the Draft Fourteenth Directive.[24]

This controversy was raised as a prominent issue during the most recent meetings of the ICLEG in 2017, probably due to the influence of the *Polbud* case.[25] These debates were triggered by Advocate General Kokott's position, under discussion at the time, on whether or not to impose — and to what extent — some sort of so-called "soft" real seat theory: the requirement of an "effective economic link" (not the central administration or head office, which would be required to follow a "hard" or "pure" real seat theory) in order to avoid the creation of letterbox companies through a cross-border conversion. While some experts considered that Member States should have — or, rather, keep — the option to decide whether or not they wish to impose restrictions on outgoing companies (be it a genuine economic link or head office),[26] others expressed the view that restrictions should be mandatory.[27]

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24 While some recent studies support the adoption of the incorporation theory: *Cross-Border Mergers and Divisions, Transfers of Seat: Is There A Need to Legislate*? (2016), (34), for some others the requirement of unity of seats or, at least, a genuine link at the European level is a "must" for any cross-border conversion draft directive: see the 4th Congress of Notaries of Europe: https://www.notariesofeurope-congress2017.eu/wp-content/uploads/2017/10/TEMA-2_es_def.pdf.

25 Case C-106/16 *Polbud*, EU:C:2017:804.

26 Currently, our ECJ accepts (within Arts. 49 and 54 TFEU) that a Member State can voluntarily impose restrictions for those companies that pretend to be incorporated into its territory (i.e., companies that want to transfer their registered seat to its territory). See infra footnote 30.

27 See ICLEG Minutes from 26th February, 2016, 27th June, 2016 and, specially, 14 and 15th of June, 2017 and 10 and 11th of July, 2017.

2. *After Polbud: The Proposal's Anti-Abuse Clause on "Artificial Arrangements"*

a. The Polbud Judgment

After the last meeting of the ICLEG with the Commission (October 4th 2017), the judgment on *Polbud* was delivered (October 25th 2017) and, as it is known, the ECJ endorsed the grounds of the "incorporation theory" (allowing any company to freely chose a company law more suitable for itself). The discussion on whether or not to include the "effective economic link" in any draft directive on cross-border conversions was clearly over after this judgment. As the Explanatory Memorandum of the Proposal notes out, the ECJ has stated very clearly that no effective economic link or activity can be required for the cross-border conversion to be effective:

> "*The ECJ held that the freedom of establishment is applicable when the registered office alone, without the real head office, is transferred from one Member State to another if the Member State of new incorporation accepts the registration of a company even without the exercise of an economic activity there: in that case Article 49 TFEU does not require such an economic activity as a precondition for its applicability* ".[28]

However, the *Polbud* judgment is not so different from its precedents. Its doctrine "gets back to the basics" in regards to the limits for each Member State for imposing rules or restrictions for cross-border conversion.[29] The ECJ confirmed its previous jurisprudence in *Polbud* allowing restrictions to the extent that: (1) they were permitted by the Treaty derogations (in particular: Arts. 51 and 52 TFEU); (2) they were justified by overriding requirements in the public interests according to the so-called "*Gebhard* test"[30] (any restriction must be appropriate to protect those interests and must not go beyond what is needed to achieve that objective); or (3) in the

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28 Proposal's Explanatory Memorandum (2).

29 As the *Polbud* case recalls, in the absence of harmonization, Member States are competent to decide the connecting factor of a company to its national order and thus apply their own incorporation requirements to incoming companies (*Polbud – Wykonawstwo*, Case C-106/16, ECLI:EU:C:2017:804, para 40; *Daily Mail and General Trust*, 81/87, EU:C:1988:456, paras 19 to 21; *Cartesio*, C-210/06, EU:C:2008:723, paras 109 to 112; *VALE*, C-378/10, EU:C:2012:440, para 32).

30 Named in this way after the ECJ judgment of 30.11.1995, *Gebhard* case C-55/94, ECLI:EU:C:1995:411, para 37.

case of abuse of the freedom of establishment ("wholly artificial arrangements" within the meaning of the *Cadbury Schweppes* judgment).[31]

This context explains why the Proposal, abandoning any effective economic link requirement with the Member State of destination, has introduced a general anti-abuse clause well known in the tax law field and ECJ jurisprudence: the so-called artificial arrangements. As we will see below, this general clause, which aims to prohibit the abusive use of cross-border conversion procedures, is not so far away from the postulates of what it has been previously called a "soft" real seat theory in relation to Advocate General Kokott's position.

b. The ECJ's Tax Doctrine Behind the "Artificial Arrangement" Anti-Abuse Clause

In the judgment on *Cadbury Schweppes*[32] (following the previous case *Lankhorst*),[33] the ECJ expressed its position regarding the adequacy of the rules on "controlled foreign companies" with the freedom of establishment enacted by the Treaty.[34] In its judgment, the court stated that "*the fact that the company was established in a Member State for the purpose of benefiting from more favourable legislation does not in itself suffice to constitute abuse of that freedom*" (para 37). However, the court made an assertion more significant for the purpose of this paper in para 51:

> "*On the other hand, a national measure restricting freedom of establishment may be justified where it specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the Member State concerned*[35]".

The analysis of this concept (a "wholly artificial arrangement"), incorporated previously by the ECJ in *Lankhorst* case, is deliberately indeterminate and has raised many doubts among both Spanish and international

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31 ECJ judgment of 12.9.2006, *Cadbury Schweppes*, Case C-196/04, ECLI:EU:C:2006:544, paras 51ff, 68, 72, 75.

32 CJEU, 12.9.2006, *Cadbury Schweppes*, Case C-196/04.

33 CJCE, 12.12.2002, *Lankhorst-Hohorst*, C-324/2000.

34 Jose M. Almudí, "El régimen antielusivo de transparencia fiscal internacional", en (dir. F. Serrano) *Fiscalidad internacional*, www.cef.es, (2015), 1037 (1195 et seq.).

35 The judgment referred to previous decisions: Case C-324/00 *Lankhorst-Hohorst* [2002] ECR I-11779, para 37; *De Lasteyrie du Saillant*, para 50; and *Marks & Spencer*, para 57.

tax doctrine. Thus, perhaps, the greatest merit of the *Cadbury* judgment is to specify a little more of its content when clarifying the advent of a wholly artificial arrangement dependent on the fact that the company obtaining a tax advantage actually pursues "*an economic activity through a fixed establishment*" in that country. As the Court states:

> "(…) *the concept of establishment within the meaning of the Treaty provisions on freedom of establishment involves the actual pursuit of an economic activity through a fixed establishment in that State for an indefinite period (see Case C-221/89 Factortame and Others [1991] ECR I-3905, para 20, and Case C-246/89 Commission v. United Kingdom [1991] ECR I-4585, para 21). Consequently, it presupposes actual establishment of the company concerned in the host Member State and the pursuit of genuine economic activity there*".[36]

Despite the difficulties of defining such a broad concept as "actual pursuit of an economic activity", in order to assess whether a particular operation (in the present case, a cross-border conversion) is an artificial arrangement, it seems clear that the introduction of this anti-abuse clause means that the Commission has not "left aside" the real seat issue. The application of the *Cadbury*'s doctrine leads to a requirement that is not so far away from Advocate General Kokott's position in *Polbud:* while in *Polbud* an "effective economic link" of the converted company with the Member State of destination was required, in *Cadbury,* an "actual pursuit of an economic activity" was necessary.

The difficulty of defining the concept — again, deliberately broad — of the *Cadbury* judgement's doctrine underlies determining when an "actual pursuit of an economic activity" (*implantación real*)[37] exists or not. This is likely why the Proposal intends to facilitate the authority's assessment task (see below III.2) to determine whether an artificial arrangement exists, by providing a list of elements (*numerus apertus*) to take into account when

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36 Paras 54 and 66 of CJEU, 12.9.2006, *Cadbury Schweppes*, Case C-196/04.

37 Jose M. Almudí, (2015), 1037 (1225), points out that some of our neighboring countries such as France, Germany, Sweden or the United Kingdom have already begun to modify their controlled foreign companies regulations to adapt them to the *Cadbury* case. Most of them have chosen to incorporate a series of objective criteria related to proportionality into the aforementioned regulation of the material and human resources used by the entity that has participated in the development of its activity. This author ask the Spanish legislator to follow the example of those Member States, nevertheless taking into account that some activities (such as finance, intermediation, etc.) may be developed by the subsidiary with a small volume of employees and a reduced physical presence (1226).

the procedure (a so-called "in-depth assessment") is opened due to the fact that the national authority has a well-founded suspicion that the cross-border conversion might constitute an abuse (Art. 86.n). These elements, which, as the norm indicates, are only

> "*considered as indicative factors in the overall assessment and therefore shall not be considered in isolation*", are the following: "*the characteristics of the establishment in the destination Member State, including the intent, the sector, the investment, the net turnover and profit or loss, number of employees, the composition of the balance sheet, the tax residence, the assets and their location, the habitual place of work of the employees and of specific groups of employees, the place where social contributions are due and the commercial risks assumed by the converted company in the destination Member State and the departure Member State*".

Therefore, the "actual pursuit of an economic activity" required by *Cadbury* and the "effective economic link" required by General Advocate Kokott are not so different from each other; both of them point to some sort of economical bond with the Member State of destination for the reincorporated or converted company. The main difference underlying both doctrines is that this economical or material bond for a cross-border conversion expressly requires some sort of "subjective element" of abuse (or fraud) — the aim to "*obtaining undue tax advantages or unduly prejudicing the legal or contractual rights of employees, creditors or minority shareholders*" — to be applied.

However, from a legal policy approach (these technical issues will be addressed further, see III.2), the general anti-abuse clause represented by the artificial arrangements is controversial. Since the Proposal already protects the legal or contractual rights of employees, creditors or minority shareholders from any undue prejudice, in practice, it seems that the only field where this anti-abuse clause could be applied would be that of "*obtaining undue tax advantages*". Hence, it seems more appropriate that these tax law problems continue to be addressed — as they currently are — by tax law and jurisprudence, not by corporate law (especially taking into account that, from the tax law perspective, the artificial arrangement doctrine works *ex post* and "does not affect the validity of the transaction as such but combats artificial arrangements by ignoring them for tax law purposes only").[38]

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38 Being — as it has been pointed out "this targeted approach probably superior": See the accurate critical approach by ECLE, "The Commission's 2018 Proposal on

III. Harmonised Procedure and Anti-Abuse Assessment

The elaboration of a harmonised proceeding in the EU is a key tool for cross-border conversions to be (technically) possible and to offer legal certitude for the various stakeholders involved in the operation. Common procedural elements are therefore needed, not only for the conversion to be made ("enabling law perspective"), but also to provide common grounds for the protection of those stakeholders to be exercised or invoked along the lines of the conversion procedure ("protective law"). The Proposal assumes this reasoning and, as expressly indicated in the Explanatory Memorandum, aims to combine these two perspectives of legal policy:

> "*In light of the foregoing considerations, the main objectives of the harmonised rules for cross-border conversions are twofold:*
> *- enabling companies, particularly micro and small, to convert cross-border in an orderly, efficient and effective manner;*
> *- protecting the most affected stakeholders such as employees, creditors and shareholders in a suitable and proportionate manner*".[39]

To this end, the Proposal parts from the procedural framework of the so-called "European model for structural changes",[40] which was set out for the first time in the merger Directive, subsequently adopted in the divisions Directive and by the cross-border mergers Directive (the three of them now consolidated in Directive 2017/1132) and it is also present in the procedural rules on cross-border transfer of seat in Art. 8 SE Regulation and Art. 7 SCE Regulation.

1. The Phases of the Cross-Border Conversion Procedure

The Proposal provides for a conversion procedure structured in several phases, which will culminate in a double control (scrutiny) of its legality, firstly, by the authority of the Member State of origin and, secondly, by the Member State of destination's authority. Basically, as already stated, the system already existing in the current regulation of cross-border mergers is

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Cross-Border Mobility – An Assessment", September, 2018 (https://europeancompanylawexperts.wordpress.com/publications/the-commissions-2018-proposal-on-cross-border-mobility-an-assessment-september-2019/#_ftnref36).

39 Proposal's Explanatory Memorandum (3).

40 Suggested, among many others, by Jessica Schmidt in *Cross-Border Mergers and Divisions, Transfers of Seat: Is There A Need to Legislate?* (2016) (9).

followed by and — with the necessary adjustments and improvements — is transferred to both the procedural model of conversions and divisions drafted by the Proposal. This model involves articulating the operation in three phases.

a. Preliminary Phase: Conversion Draft and Reports

In the first phase, the management body will prepare the draft terms on the cross-border conversion. This draft will be joined by two reports, also prepared by the same organ, to be delivered to the shareholders (Art. 86.e) and to the employees (Art. 86.f), dealing with the implications that the conversion will have for them as well as remedies for their protection. The report for the shareholders may be waived if all of them agree.

The conversion draft terms, which must be made public at least one month before the general meeting (Art. 86.h), must contain some minimum information (Art. 86.d) regarding the change of the company's legal form as well as the protection offered to shareholders, creditors and employees. The Proposal (Art. 86.d) also offers companies the possibility to provide the draft terms in the official languages of the Member States concerned, as well as in the language most commonly used in business transactions (presumably English). In this sense, Member States will be able to determine which language is preferable in case of discrepancies.

In this first phase, it is worth noting that the preparation of a report by an independent expert (Art. 86.g) is also mandatory — though only for medium and large companies[41] — and its appointment will have to be requested by the company from the competent authority (in Spain, this will be the mercantile register). The independent expert's report must examine the accuracy of the draft terms and reports prepared by the management body. This requirement, logically, will increase the cost of the operation, but it plays a central role in the procedure defined by the Proposal since this independent expert will provide the factual basis for the assessment to be carried out by the authority on the risk that the operation could be abusive (that is, on the risk that it constitutes an artificial arrangement, see below 2).

41 As Art. 86.g para 6 states: "Member States shall exempt 'micro' and 'small enterprises' as defined in Commission Recommendation 2003/361/EC (**) from the provisions of this Article."

The conversion draft, the management reports and, if the case requires, the independent expert report, will be made available to the public for free [Art. 86.h)6º][42] and completely online [Art. 86.h)4º]. Besides, shareholders, creditors and employees may submit any comments on them, before the date of the general meeting, to the company and to the competent authority [Art. 86.h)1º, 4º].

b. The Resolution on Conversion and Protection Remedies

From that moment on, the second phase of the operation opens up. This is built, on the one hand, around the adoption of a resolution by the general meeting on the approval of the draft terms (Art. 86.i) and, on the other hand, around the eventual exercise of the rights that the Proposal recognises in terms of those stakeholders who might be adversely affected by the cross-border conversion: minority shareholders dissatisfied with the conversion (Art. 86.j), creditors (Art. 86.k) and employees (Art. 86.l) (as for those rights, see in detail below IV).

The Proposal requires the resolution of the general meeting to be adopted by a qualified majority ("*Member States shall ensure that the approval of any amendment to the draft terms of the cross-border conversion requires a majority of not less than two-thirds*"), expressly imposing a maximum threshold [Art. 86.i)3º] of 90% of the voting rights ("*but not more than 90% of the votes attached either to the shares or to the subscribed capital represented*"), oriented to prevent unanimity from being demanded by any Member State (as occurs under French law). The provision also requires that "*In any event the voting threshold shall not be higher than that provided for in national law for the approval of cross-border mergers*." A few comments can be drawn out from the current wording of the provision.

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42 The European Commission aims to reduce publicity costs associated with these kind of cross-border transactions. Thus, para 6 of Art. 86.h states: "*Member States shall ensure that the documentation referred in paragraph 1 is accessible by the public free of charge*." However, the MMSS may "*require, in addition to the disclosure referred to in paragraphs 1, 2 and 3, that the draft terms of the cross-border conversion, or the information referred to in paragraph 3 is published in their national gazette (…)*", and, if such is the case, "*Member States shall further ensure that any fees charged to the company carrying out the cross-border conversion by the registers for the disclosure referred to in paragraphs 1 and 3 and, where applicable, for the publication referred to in paragraph 5 shall not exceed the administrative costs of providing the service*".

Firstly, the mention of "*the approval of any amendment to the draft terms*" might be the result of a "typo", since the provision is aimed to regulate the approval of the transaction by the general meeting (and, if it is the case, its amendments).[43] Thus, "of" should be replaced with "or", in order to establish that "*Member States shall ensure that the approval* or *any amendment to the draft terms…*".

Secondly, from the perspective of Spanish law — in regards to its future implementation — the current drafting of Art. 86.i)3º could raise some technical difficulties when confronting the rule on the minimum qualified majority (not less than two-thirds) with the rule (in the same provision) that requires the voting threshold to not be higher than the one provided for in national legislation for the approval of cross-border mergers. Although this provision apparently follows the current Directive 2017/1132 (Art. 93.1), an important statement — at least from the Spanish law perspective — is missing in the current Proposal: the one that allows that, under certain conditions, a simple majority may suffice (see Art. 93.1 subpara 2º).[44] Indeed, the simple majority is the voting threshold (under certain conditions for public limited companies in Spain, Art. 201.2º LSC) for these kind of transactions under Spanish law (see Arts. 40 and 97 LME for national mergers and transfer of seat, both referring to Art. 201 LSC).

c. The Two-Pronged Scrutiny

Finally, as part of the third phase of the cross-border conversion, the resolution of the general meeting, together with the relevant information and documents, will be submitted to the national authority of the Member State of origin, which will decide whether to issue a certificate of "pre-conversion". This phase is built upon a two-pronged scrutiny or double control of the legality of the transaction. While Arts. 86.m (pre-conversion certificate) and 86.n (in-depth assessment) refer to the control task in the Mem-

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43 This possibility (the "amendment" of the draft terms is not permitted under current Spanish law neither for (national or cross-border) mergers nor cross-border transfer of seat (see Art. 40.1 LME, for mergers and applicable for cross-border mergers and transfer of seat).

44 This subparagraph says: "The laws of a Member State may, however, provide that a simple majority of the votes specified in the first subparagraph shall be sufficient when at least half of the subscribed capital is represented. Moreover, where appropriate, the rules governing alterations to the memorandum and articles of association shall apply.".

ber State of origin, Art. 86.p (scrutiny of the legality of the cross-border conversion) regulates the revision by the authority of the Member State of destination. These are rules that, in short, reproduce the scheme and the principles already foreseen in the SE Regulation and in the rules regarding cross-border mergers (Arts. 117 and 128 Directive 2017/1132).

With regard to this first control (the one made by the Member State of origin's authority), the aforementioned provisions require two tasks: (1) to assess whether or not the formal procedure of the cross-border conversion has been made in accordance with the provisions of its national legislation; and (2) whether or not the operation constitutes an artificial arrangement. To carry out these tasks, the national authority counts with a maximum period of one month that might be extended, if there are well-founded suspicions that the conversion is abusive, i.e. "artificial" (see below 2), to another two more months.

If the national authority issues the pre-conversion certificate after such analysis, this will then be sent to the authority of the Member State of destination (Art. 86.p), who will then carry out an examination of the part of the procedure governed by its legislation, ensuring that the converted company adheres to its national regime on incorporations (minimum capital, contributions, requirement — if it is the case — that the company has its real seat in its territory, etc.) and, where appropriate, that the arrangements for employee participation have been determined in accordance with Art. 86.l).

Once the double control of the legality has finished, the company will be registered in the Member State of destination and its registration in the Member State of origin will be cancelled (Art. 86.q). The cross-border conversion will then have legal effects (Art. 86.s) and it cannot be declared void (Art. 86.u). The ground supporting this latter provision — already known in the field of cross-border mergers — is to guarantee the legal certainty of these kind of complex transactions in which several Member States are involved. It is presumed that the *ex ante* control to which the conversion is submitted should offer a total guarantee that it complies with the legal requirements and is not fraudulent and, therefore, cannot be challenged.[45]

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45 Segismundo Álvarez, "The Commission's Company Law Package: Overview and Critical View of the Proposal for Cross-Border Transactions" (2018) (https://europeanlawblog.eu/2018/06/07/the-commissions-company-law-package-overview-and-critical-view-of-the-proposal-for-cross-border-transactions) criticises this provision saying it supposes a kind of "blessing" of the operation, even if the company had