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Unternehmensgruppen in mittel- und osteuropäischen Ländern

Entstehung, Verhalten und Steuerung aus rechtlicher
und ökonomischer Sicht

herausgegeben von
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und Katharina Pistor

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Vorwort

Während Unternehmensgruppen in Westeuropa Gegenstand intensiver, auch rechtsvergleichender Forschung und lebhafter rechtspolitischer Diskussionen sind, lassen sich Kenntnisse über Unternehmensgruppen in mittel- und osteuropäischen Ländern, wenn überhaupt, dann häufig nur mit beträchtlichem Aufwand und jedenfalls bisher nur für einzelne Länder gewinnen. Dabei stehen die Transformationsländer vor ähnlichen Aufgaben, nicht nur was den Aufbau einer funktionierenden marktwirtschaftlichen Ordnung betrifft, sondern auch bei der Vorbereitung auf den erstrebten Beitritt zur Europäischen Union. Angesichts dieser Situation hat das Max-Planck-Institut vom 22.-24. Juni 2000 führende Wissenschaftler aus einer ganzen Reihe von mittel- und osteuropäischen Ländern, aber auch aus Westeuropa zu einem Symposium nach Hamburg eingeladen, um gemeinsam eine Bestandsaufnahme der Ursachen für die Entstehung von Unternehmensgruppen in Transformationsländern, ihr Verhalten sowie ihre mögliche Steuerung mittels rechtlicher Instrumentarien bzw. ökonomischer Anreizstrukturen zu untersuchen. Die auf dem Symposium gehaltenen Vorträge werden in diesem Band der Öffentlichkeit vorgelegt, unter Berücksichtigung zwischenzeitlicher Rechtsänderungen. Die Veranstaltung wurde zweisprachig durchgeführt, so dass einige Referate in deutscher, andere in englischer Sprache abgefasst sind. Die unterschiedlichen Themenstellungen ergeben sich aus der Gliederung des Symposiums in die Abschnitte: Unternehmensgruppen im Ländervergleich; derzeitige Steuerung von Struktur und Verhalten von Unternehmensgruppen; Anleger- und Gläubigerschutz in Unternehmensgruppen; Finanzinstitutionen als Teil von Unternehmensgruppen; Unternehmensgruppen, selbststeuernde Prozesse und Wettbewerb. Ziel des Symposiums war es, über die bloße Information hinaus gemeinsam Vorschläge für die zukünftige Behandlung der Unternehmensgruppen in Mittel- und Osteuropa zu entwickeln. Sie sind im 7. Abschnitt des Beitrages von Hopt/Pistor (S. 32 ff.) enthalten.

Hamburg, im November 2002

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Abkürzungsverzeichnis

ABl	Amtsblatt
AG	Aktiengesellschaft/Die Aktiengesellschaft. Zeitschrift für das gesamte Aktienwesen
AktG	Aktiengesetz
APAPS	Agency of Privatisation
BB	Der Betriebs-Berater
Bd.	Band
BG	Bulgarien
BGBI.	Bundesgesetzblatt
BGH	Bundesgerichtshof
BGHZ	Entscheidungen des Bundesgerichtshofes in Zivilsachen
BiH	Bosnien und Herzegowina
BKartA	Bundeskartellamt
BT-Drucks.	Bundestagsdrucksache
Cah.dr.fisc.intern.	Cahiers de droit fiscal international
Cass. Crim.	(Arrêt de la) Cour de Cassation, Chambre criminelle
CEECs	Central and Eastern European Countries
CNVM	National Securities Commission
CS	Tschechische Republik und Slowakische Republik
DB	Der Betrieb
dr.	droit
DStR	Deutsches Steuerrecht
dt.	deutsch
D.V.	Dáržaven Vestnik
Dz.U.	Dziennik Ustaw
EBOR	European Business Organization Law Review
EBRD	European Bank for Reconstruction and Development
EC	European Communities/EC Treaty
ECE	Economic Commission for Europe
ECJ	European Court of Justice
ECLR	European Competition Law Review
ECR	European Court Reports
ECSC	European Coal and Steel Community
ed.	Edition
ed(s).	Editor(s)
EEC	European Economic Community
EG	Europäische Gemeinschaften
EGV	EG-Vertrag; Vertrag zur Gründung der Europäischen Gemeinschaft
EU	European Union/Europäische Union
Euratom	Europäische Atomgemeinschaft
EuZW	Europäische Zeitschrift für Wirtschaftsrecht
EWG	Europäische Wirtschaftsgemeinschaft
EWS	Europäisches Wirtschafts- und Steuerrecht
EZB	Europäische Zentralbank
FIW	Forschungsinstitut für Wirtschaftsverfassung und Wettbewerb

FOWI	Forschungsinstitut für Mittel- und Osteuropäisches Wirtschaftsrecht, Wirtschaftsuniversität Wien
FS	Festschrift
FTC	Federal Trade Commission
G	Gesetz
GDP	Gross domestic product
GDR	German Democratic Republic
GmbH	Gesellschaft mit beschränkter Haftung
GmbHR	GmbH-Rundschau
GöAW	Gesetz über das öffentliche Angebot von Wertpapieren
GRUR Int.	Gewerblicher Rechtsschutz und Urheberrecht. Auslands- und internationaler Teil
GSW	Gesetz zum Schutz des Wettbewerbs
GWB	Gesetz gegen Wettbewerbsbeschränkungen
HGB	Handelsgesetzbuch
Hrsg.	Herausgeber
idF	in der Fassung
JZ	Juristen-Zeitung
KRO	Kroatien
L.	Law
LCC	Law on Commercial Companies
LS	Law on Securities
M.K.	Magyar Közlöny
NASDAQ	National Association of Securities Dealers Automated Quotations
NJW	Neue Juristische Wochenschrift
N.n.	Narodne novine
NPIFs	National Privatization Investment Funds
NRG	Nationale Rechnungslegungsgrundsätze
NZG	Neue Zeitschrift für Gesellschaftsrecht
OCCP	Office for Competition and Consumer Protection
OECD	Organization for Economic Cooperation and Development
OJ	The Official Journal of the European communities
OLG	Oberlandesgericht
PL	Polen
RegE	Regierungsentwurf
Rev.	Revue
RIW	Recht der internationalen Wirtschaft
ROL	Rumänische Lei
RS	Republik Slowenien
Rus	Rußland
s.	section
SH	shareholder
Slg.	Sammlung
SOF	State Ownership Fund
SR	Sozialistische Republik
StGB	Strafgesetzbuch
SZ RF	Sobranie zakonodatel'stva Rossijskoj Federacii
tsch.	tschechisch
Ukr	Ukraine
USD	US-Dollar
VAT	Valueadded tax
WettbG	Wettbewerbsgesetz
WGO-MfOR	WGO-Monatshefte für Osteuropäisches Recht

WiRO	Wirtschaft und Recht in Osteuropa
WM	Zeitschrift für Wirtschafts- und Bankrecht, Wertpapiermitteilungen
WOS	Wirtschaftsrecht der osteuropäischen Staaten (Loseblatt)
WpÜG	Wertpapiererwerbs- und Übernahmegesetz
WSE	Warsaw Stock Exchange
WuW	Wirtschaft und Wettbewerb
WuW/E	Wirtschaft und Wettbewerb, Entscheidungssammlung
Yale L.J.	The Yale Law Journal
ZEuP	Zeitschrift für Europäisches Privatrecht
ZGD	Zakon o gospodarskih družbah (Gesetz über Wirtschaftsgesellschaften)
ZGR	Zeitschrift für Unternehmens- und Gesellschaftsrecht
ZHR	Zeitschrift für das gesamte Handels- und Wirtschaftsrecht
ZIP	Zeitschrift für Wirtschaftsrecht; bis 1982: Zeitschrift für Wirtschaftsrecht und Insolvenzpraxis
ZPO	Zivilprozeßordnung

Company Groups in Transition Economies: A Case for Regulatory Intervention?*

KLAUS J. HOPT and KATHARINA PISTOR

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Company groups are an important factor in transition economies. For some, the origins can be traced to the socialist period. Others are a product of the transition process. This paper discusses the likely impact of company groups on transition economies both in the short and in the long term. It suggests that while in the short term company groups may well be transaction enabling, in the long term they could create substantial costs by impeding competition and undermining the adaptability of companies to changing economic conditions. Regulatory intervention should balance the short-term benefits of company groups with their potential long-term costs. In the short term, the primary goal of regulatory intervention should be to prevent the development of structures that may be difficult to reverse and to ensure minimum protection of shareholder and creditor rights primarily through disclosure requirements and exit options. The regulation of intra-group relations based on complex legal doctrines that rely heavily on judicial evaluations as currently suggested for the European Union do not seem appropriate for transition economies, given the weakness of legal institutions in these countries.

* Revised version of the preprint in EBOR vol. 2 (2001/1).

I. Introduction

The field of comparative corporate governance is currently undergoing what may amount to a paradigm shift. Since the seminal analysis of the modern corporation by Berle and Means in 1932,¹ the large publicly held corporation with dispersed shareholders as owners unable to effectively control management has dominated the field not only in the United States, the origin country of the Berle & Means corporation, but also elsewhere. Recent empirical analyses, however, document that the corporation with dispersed owners is much less common than typically assumed.² As a result, many of the assumptions that have driven the analysis of the corporate sector in the past are currently undergoing review.³ To a large extent, the fresh look at the corporation, its ownership structure and performance, and the legal framework in which it operates can be attributed to the recent experience of the transition economies. Reform strategies that were implemented in these countries over the past decade included the reorganization of state owned enterprises into marketable share companies and their subsequent privatization. Corporatization and privatization were expected to lead to enterprise restructuring and improved performance.⁴ In fact, these expectations materialized only slowly, if at all, and, as will be further discussed below, the emerging enterprise structures in these countries looks quite different from earlier predictions. Cynics may say that these countries became the testing ground for empirically unfounded corporate finance theories. In fact, many privatization programs in transition economies were designed and

¹ Berle and Means, *The Modern Corporation and Private Property* (New York 1932).

² La Porta, Lopez-de-Silanes and Shleifer, 'Corporate Ownership Around the World', 54 *Journal of Finance* (1999) 471; for the United States, see also Holderness, Kroszner and Sheehan, 'Were the Good Old Days that Good? Changes in Managerial Stock Ownership Since the Great Depression', 54 *Journal of Finance* (1999) 435.

³ There has been a flood of analysis by economists of ownership structures both theoretically and empirically. See only the contributions in Morck (ed.), *Concentrated Corporate Ownership* (Chicago, 2000). For a different perspective, which claims convergence on the Berle & Means corporation as a result of international financial market competition, see however Hansmann and Kraakman, *The End of History for Corporate Law*, Working Paper, Yale International Institute of Finance (2000).

⁴ There is a huge amount of literature on the pros and cons on privatization and the best approach in transition economies. For the early debate, see Lipton and Sachs, *Privatization in Eastern Europe: The Case of Poland*, Brookings Papers on Economic Activity (1990) p. 293 and Frydman and Rapaczynski, 'Markets and Institutions in Large Scale Privatization: An Approach to Economic and Social Transformation in Eastern Europe', in: Corbo, Coricelli and Bossak (eds.), *Reforming Central and Eastern European Economies: Initial Results and Challenges* (Washington, D.C. 1992) 253. For a review of mass privatization and the results, see Pistor and Spicer, 'Investment Funds in Mass Privatization and Beyond', in: Lieberman, Nestor and Desai (eds.), *Between State and Market: Mass Privatization in Transition Economies* (Washington, D.C. 1997) as well as other contributions in this volume. See also Pistor, 'Company Law and Corporate Governance in Russia', in: Sachs and Pistor (eds.), *The Rule of Law and Economic Reform in Russia* (Boulder, Col. 1997) 165.

advised by US trained financial economists who have now taken the lead in challenging the very same assumptions on which their advice had been based.⁵ While they earlier predicted that institutions will follow the market,⁶ they now argue that institutions, in particular legal institutions, are determinants of the ownership structure of firms and the development of capital markets.⁷ In any event, the process of transforming centrally planned economies into market economies has revealed how little is understood about markets and firms or the role of law and legal institutions for their functioning.

Against this background, the Max Planck Institute for Foreign Private and Private International Law in Hamburg hosted a symposium on company groups in transition economies in June 2000. The choice of topic was motivated by the observation that the company structure that is currently emerging in transition economies is characterized more by concentrated ownership, the formation of company groups and network relations among firms, than by independent firms with dispersed shares. The symposium brought together experts from various transition economies, including Bulgaria, Croatia, the Czech Republic, Hungary, Poland, Romania, Russia, and Slovenia, as well as from Western Europe. The goal of the symposium was to take stock of the importance of company groups in these countries, the legal problems that arise from the existence or even dominance of groups, and to discuss possible approaches to legal and institutional reforms.

In this paper, we summarize available data on company groups and discuss legal issues that arise with company groups. In particular, we assess legal solutions that are currently practiced in developed market economies in light of the institutional infrastructure of transition economies. This paper will be followed by articles that highlight specific aspects of company groups in transition economies. We hope that their publication will make the problems currently faced by transition economies accessible to a broader audience.

This paper is organized as follows. Section II presents a typology of company groups in transition economies as well as available empirical data. Section III reviews some economic explanations for the emergence of company groups and assesses their relevance for transition economies. In section IV we discuss the key legal issues that arise with company groups, including competition law and the protection of shareholder and creditor rights. Section V gives an over-

⁵ This is true in particular for the design of the Russian privatization program. The leading advisors were Professors Andrei Shleifer of Harvard and Robert Vishny of Chicago University. See Boycko, Shleifer and Vishny, *Privatizing Russia*, Brookings Papers for Economic Activity (1993) p. 139 and more recently La Porta, Lopez-de-Silanes, Shleifer and Vishny, 'Law and Finance', 106 *Journal of Political Economy* (1998) 1113; La Porta, Lopez-de-Silanes, Shleifer and Vishny, 'Legal Determinants of External Finance', 52 *Journal of Finance* (1997) 1131 and La Porta et al. (1999), *supra* n. 2.

⁶ Boycko, Shleifer and Vishny, *Privatizing Russia* (Cambridge, Mass. 1995).

⁷ See La Porta et al. (1997) and (1998), *supra* n. 5.

view of issues that arise when financial institutions, in particular banks, are part of company groups. Section VII concludes with our propositions for regulating company groups in transition economies.

II. Typology and empirical evidence

Company groups are not a new phenomenon in transition economies. Conglomerates or associations of firms were a key characteristic of centrally planned economies. As plan fulfillment remained an unresolved problem, companies increasingly produced their own supplies, or established close ties with companies in the same production chain through enterprise associations. Moreover, the central administration found it easier to manage fewer large conglomerates or associations than a larger number of freestanding firms.⁸

New conglomerates joined these remnants of the classic socialist system during the period of reform socialism. In an attempt to revive their faltering planned economies, many countries decentralized economic decision-making to the company level. This process was most pronounced in Hungary, where it started already in the late 1960s.⁹ During the period of *perestroika* it also affected companies in the former Soviet Union. Other countries, however, remained unaffected. This is true in particular for the Czech Republic and Eastern Germany, where central economic administration prevailed until the collapse of the regime.¹⁰ The effect of decentralization was that company management took over control of assets, while trying to shift liabilities to the state as the still *de jure* owner. This process has been termed 'spontaneous privatization'. When management created subsidiaries or joint ventures with foreign parties and shifted valuable resources and production lines to these new entities, this resulted in the formation of a company group. The regime change did not halt the process of spontaneous privatization, but in many cases accelerated it, as the

⁸ For a discussion of conglomerates (*obyedineniye*) in the Soviet Union, compare Nove, *The Soviet Economic System* (London 1986), especially p. 75; and Kornai, *The Socialist System: The Political Economy of Communism* (Princeton, N.J. 1992) p. 399. Note that the policies towards concentration changed over time. In the Soviet Union, the 1960s in particular witnessed some decentralization. Nevertheless, large fully or partially integrated company groups remained a feature of the socialist system.

⁹ For an analysis of this and comparable reform strategies in other socialist countries, which went under the rubric of 'market socialism', compare Kornai, *The Road to a Free Economy – Shifting from a Socialist System* (New York/London 1990) p. 57 with further references; and Kornai (1992), *supra* n. 8 at p. 383.

¹⁰ For a comparison of pre-reform strategies and their affinity with post socialist reform agendas, compare Stark and Brusz, *Postsocialist Pathways: Transforming Politics and Property in East Central Europe* (Cambridge, UK, 1998) p. 80. See also Elster, Offe and Preuss, *Institutional Design in Post-communist Societies: Rebuilding the Ship at Sea* (Cambridge, UK 1998) p. 35.

new policies created a run for assets.¹¹ The creation of an official and legally regulated privatization process thus did not mark the beginning of privatization, but an attempt to base it on orderly procedures.

Many observers noted the concentration of economic power in the former socialist countries at the outset of the reform process. Some suggested that these structures needed to be unbundled before privatization could proceed,¹² while others argued that the integration of these economies into the world market would diminish the influence of domestic conglomerates especially in the smaller countries of Central and Eastern Europe.¹³ In some countries, privatization led to spin-offs of individual firms from larger conglomerates, and thus resulted in some unbundling. Given the speed with which privatization strategies were implemented, however, this process remained incomplete. In fact, proponents of rapid privatization strategies did not view favorably interventions by antitrust agencies in the privatization process.¹⁴

Whatever the merits of restructuring prior to privatization, it soon became apparent that company groups were not only a legacy of the past. The transition process also led to the creation of new company groups, or business networks. They can be classified as 'privatization groups' in case privatization strategies led to the creation of company groups; as 'oligarch groups', when company groups were formed around influential individuals closely involved in the political and economic power battles; or as 'restructuring networks'. The latter term, which is borrowed from David Stark,¹⁵ refers to the process of the emer-

¹¹ Johnson and Kroll, 'Managerial Strategies for Spontaneous Privatization', 7 *Soviet Economy* (1991) 281; Voszka, 'Spontaneous Privatization in Hungary', in: Earle, Frydman and Rapaczynski (eds.), *Privatization in the Transition to a Market Economy* (London 1993) 89.

¹² Brzezinski, 'Competition and Antitrust Law in Central Europe: Poland, the Czech Republic, Slovakia, and Hungary', *Michigan Journal of International Law* (1994) 1129 and Mastalir, 'Regulation of Competition in the New Free Markets of Eastern Europe: A Comparative Study of Antitrust Law in Poland, Hungary, Czech and Slovak Republics, and their Models', 19 *North Carolina Journal of International Law and Commercial Regulation* (1993) 61.

¹³ Lipton and Sachs, *Creating a Market Economy in Eastern Europe: The Case of Poland*, Brookings Papers on Economic Activity (1990) p. 75. This economic advice notwithstanding, it was Poland that established the strongest antitrust agency in the region. For details see Fornalczyk, in this volume pp. 179.

¹⁴ For a discussion of the tensions between decentralization on the one hand, and depoliticization, which was thought to be achievable through privatization, see Joskow, Schmalensee and Tsukanova, *Competition in Russia During and After Privatization*, Brookings Papers: Microeconomics (1994) p. 335, and especially p. 343. They argue that privatization has ultimately benefited decentralization. This judgment, however, at least with hindsight appears to be premature. Certainly the privatization of the large natural resource companies in 1995, i.e., after the article had been published, resulted in a substantial concentration of economic power. See Johnson, 'Russia's Emerging Financial-Industrial Groups', 13 *Post-Soviet Affairs* (1997) 333.

¹⁵ Stark and Brusz, *supra* n. 10, ch. 5 at p. 137. See also Stark, 'Networks of Assets, Chains of Debt - Recombinant Property in Hungary', in: Frydman, Gray and Rapaczynski

gence of company groups with privatized or newly private firms as their members in response to the economic and institutional environment they faced. Finally, as foreign strategic investors participated in privatization or acquired private or privatized firms, companies in transition economies became part of what we call transnational company groups – a well-known phenomenon within the European Union, and a growing phenomenon internationally.¹⁶

The purpose of our typology of company groups is to remind us that the existence of company groups in transition economies can be traced to different factors. Any theory that attempts to explain company groups in these countries must address the different legacies of these groups. Even more importantly, suggestions for regulatory intervention should be critically assessed as to whether they can possibly provide effective remedies in light of the causes that gave rise to the emergence of these groups.

Empirical evidence on company groups in transition economies remains scant and for the most part anecdotal.¹⁷ The different types of company groups identified above, can be found in every transition economy, but incidence of particular types of groups (i.e., socialist groups, *perestroika* groups, privatization, oligarch, network restructuring, or transnational groups) differs from country to country.¹⁸

In an attempt to base our analysis on more systematic data, we have assembled data on the ownership structure and the identity of owners of the largest companies in several transition economies. Ownership concentration is not identical with company groups.¹⁹ Ownership concentration can, however, be taken as a first approximation of the existence of company groups, as large equity stakes held by other corporations are suggestive of a strong formal tie between at least two companies. The identity of owners reveals whether block-

(eds.), *Corporate Governance in Eastern Europe and Russia*, Vol. 2 (London/Budapest/New York 1996) 109.

¹⁶ Transnational or multinational enterprises (MNEs) have been around for a while. There is a vast amount of literature on them. However, the scale of transnational mergers, including mergers of which neither party is a firm from the United States is of more recent origin. Compare Black, 'The First International Merger Wave (and the Fifth and Last U.S. Wave)', 54 *University of Miami Law Review* (2000) 799. A prominent example is the takeover of Mannesmann by Vodafone in 2000.

¹⁷ Many of the contributions at the symposium presented evidence of company groups from court cases or antitrust proceedings, but nobody had access to systematic data. Perhaps, this is not so surprising. Recall that it took a special effort by the European Corporate Governance Network (ECGN) to produce systematic data on ownership concentration in Western Europe. See Becht and Roell, 'Blockholdings in Europe: An International Comparison', 43 *European Economic Review* (1999) 1049.

¹⁸ For evidence on the persistence of socialist and *perestroika* groups in Russia compare Broadman, 'Reducing Structural Dominance and Entry Barriers in Russian Industry', 17 *Review of Industrial Organization* (2000) 155.

¹⁹ For a more detailed analysis of the relationship between these two concepts, see *infra* III.A.

holders are primarily domestic or foreign firms, or whether they are strategic or financial investors – a distinction that is relevant for our discussion of financial institutions as part of company groups.²⁰ Given the higher disclosure requirements for publicly traded companies, data for these firms are best accessible.²¹ Data are available only for three of the transition economies represented at the symposium, namely the Czech Republic, Hungary and Poland. We include the largest non-financial firms among the largest fifteen companies in the database and classify their owners as domestic financial and non-financial companies, foreign financial and non-financial companies, or the state.

The results presented in the Appendix are striking. The data reveal substantial levels of ownership concentration. For the ten Czech firms, the largest single shareholder holds on average 56.3 percent of voting stock, and the largest three shareholders together close to 80 percent. For Hungary and Poland, the levels are much lower and close to average in worldwide comparison.²² In Hungary, the largest single shareholder holds on average 27.25 percent (data for seven firms), while the three largest shareholders hold 42.33 percent. In Poland, the respective data for six firms is 27.76 percent for the largest owner and 48.77 percent for the three largest shareholders together.

Even more striking is the identity of the owners. In the Czech Republic, in seven out of ten firms, the state is still the largest shareholder;²³ in two cases it is a foreign non-financial investor, and in one a domestic non-financial investor. In Hungary, the state is the largest owner in two out of seven companies, in three it is a foreign investor, and in two a domestic company. In Poland, the state appears only in one case as the largest owner, foreign investors in three cases, of which one is a financial investors, and domestic in two.

Obviously, the data have to be evaluated with great caution. They may not be representative for the country as a whole, as the incidence of company groups among closely held companies may differ from publicly traded ones. Moreover, the strong presence of the state as an owner in the Czech Republic may overstate the extent of continuous state ownership in this country in comparison with the other two. It may simply reflect the fact that in the Czech Republic all companies that went through mass privatization were automatically listed on the Prague Stock Exchange and thus found their way into the database we used.²⁴ By contrast, many of the firms with large state ownership

²⁰ See *infra* V.

²¹ Data were obtained from Bloomberg L.P. (Princeton, NJ 1992) (series).

²² See La Porta et al. (1998) *supra* n. 5, Table 7. The sample average is 46% for the stock held by the largest three shareholders based on the largest ten non-financial firms listed on the stock exchange.

²³ In part this can be attributed to the fact that utilities companies belong to the largest publicly traded companies in the Czech Republic.

²⁴ See Pistor, 'Law as a Determinant for Stockmarket Development in Eastern Europe', in: Murrell (ed.), *Assessing the Value of Law in Transition Economies* (Ann Arbor 2001) for a

in the other two countries may simply not be listed. In fact, the EBRD estimates that by the end of 1999 the total share of GDP in the private sector had reached 80 percent in the Czech Republic and Hungary but was still at 65 percent in Poland.²⁵

Despite these qualifications, the data should caution against the assumption that company groups continue to be and therefore should be treated primarily as a domestic phenomenon. If we exclude the companies that are predominantly owned by the state,²⁶ foreign strategic investors followed by foreign financial investors are the most important blockholders of the largest firms in these countries. Whatever the effects of transnational company groups on the domestic economy, the leading company of the group will be located outside the domestic jurisdiction. This is true at least for the Visegrad countries, which received over 70 percent of total flows of foreign direct investments into the former socialist countries.²⁷ Even though the incidence of transnational groups may be lower in other transition economies, the experience of the Visegrad countries may repeat itself there, as investment in the region can be explained best by multinationals pursuing global strategies in a changing world, not by specifics of these countries.²⁸

III. Theoretical explanations for the emergence of company groups

A. General observations

The analysis of company groups is a difficult task, mostly because there is no consistent body of literature about, and no common understanding of, the

comparative analysis of the development of capital markets and the relevant institutional framework in these three countries.

²⁵ EBRD, *Transition Report – Employment, Skills and Transition* (London 2000), country assessments p. 124 at pp. 156, 172, and 196.

²⁶ The state continues to be the most important parent of companies that have been privatized only partially. It may, however, be an exaggeration to label companies that are owned largely by the state and managed by an entity such as the National Property Fund in the Czech Republic, or State Holding Company (AVRt – Hungary acronym for Hungarian State Property Management Agency) in Hungary as members of a company group. Having a single state management agency does not necessarily imply that firms are subjected to a single group management strategy. In fact, available evidence suggests that the state has by and large been a rather passive owner. See Pistor and Turkewitz, 'Coping with Hydra – State Ownership After Privatization', in: Frydman et al. (eds.) Vol. 2, *supra* n. 15, at pp. 192 et seq. for an early assessment of the state as an owner in partly privatized companies.

²⁷ Krifa and Vermeire, 'L'Intégration des Pays d'Europe Centrale dans les Réseaux de Production des Multinationales et ses Conséquences', 29 *Revue d'Études Comparatives Est-Ouest* (1998) 77. They attracted more than 24 billion US dollars.

²⁸ *Ibid.*, at p. 106.

definition of a company group across existing literature.²⁹ There is extensive literature on the costs and benefits of firm concentration from a macroeconomic perspective. Similarly, there is a large volume of literature on cartels as well as on mergers, and their impact on the competitiveness of nations. By contrast, new institutional economics, including theories of the firm, have struggled to define the boundaries of the firm, but have hardly addressed the phenomenon of company groups.³⁰ Similarly, the corporate governance debate hardly mentions the concept, but instead focuses primarily on concentrated ownership. The two concepts are related, but do not overlap completely.

Concentrated ownership is the simpler concept. It means that a firm is owned by relatively few large blockholders. The relevant threshold for concentrated ownership may be debatable, and in fact may vary from country to country. Where on average shareholders hold hardly more than 5 percent of a company's shares, a 20 percent shareholder may be deemed a blockholder. By contrast, where majority owners are common, a 20 percent shareholder might not have much influence, as a stake of this size would not even give him a veto right for decisions with qualified majority.

The real debate in economics literature concerns the costs and benefits of concentrated ownership. Substantial literature has pointed to the benefits of relatively concentrated ownership, as this reduces agency costs and thus enhances corporate monitoring.³¹ Until the early 1990s, the Japanese and German corporate governance systems were viewed with envy by many American commentators. Firms seemed to benefit from concentrated ownership, which typically implied few changes in the ownership structure and thus lengthened the time horizon of management. The major cost of concentrated ownership is self-dealing by management and/or blockholders at the expense of minority

²⁹ See also Khanna, 'Business Groups and Social Welfare in Emerging Markets: Existing Evidence and Unanswered Questions', 44 *European Economic Review* (2000) 748.

³⁰ The theory that is most closely associated with explaining the boundaries of the firm is the property rights theory. For a good overview of this theory and its comparison with other theories of the firm, compare Hart, 'An Economist's Perspective on the Theory of the Firm', 89 *Columbia Law Review* (1989) 1757. For a more recent overview compare Hart, *Firms, Contracts, and Financial Structure* (Oxford 1995) p. 228.

³¹ See Jensen and Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure', 3 *Journal of Financial Economics* (1976) 305 on the nature of agency costs in firms. On the benefits of concentrated ownership see Roe, 'A Political Theory of American Corporate Finance', 91 *Columbia Law Review* (1991) 10 and Roe, *Strong Managers, Weak Owners: The Political Roots of American Corporate Finance* (Princeton, N.J. 1994). For an analysis of the tradeoffs between liquidity and control compare Coffee, 'Liquidity Versus Control: The Institutional Investor as Corporate Monitor', 91 *Columbia Law Review* (1991) 1277. Empirical data on management ownership in the United States also suggest that there may be some benefits to ownership concentration in the hands of management. Compare Morck, Shleifer and Vishny, 'Management Ownership and Market Valuation: An Empirical Analysis', 20 *Journal of Financial Economics* (1988) 293.

shareholders.³² The optimal ownership structure thus seems to lie somewhere between excessive agency costs in the case of highly dispersed ownership, and the lack of market disciplining in the case of highly concentrated managerial or blockholder ownership.

With the changing economic cycles between Germany and Japan on the one hand, and the United States and United Kingdom on the other, the assessment of corporate governance systems has shifted. Countries with relatively dispersed ownership structures and liquid markets now have taken the lead, and thus dispersed ownership structures and shareholder value are hailed as the panacea for enterprise growth and development.³³ Whether this is indeed the 'end of history', as some authors claim,³⁴ remains to be seen. The extreme swings in the recent debate suggest that not even for developed market economies a consensus has emerged as to the superiority of alternative corporate governance systems. Therefore, caution is in order when applying these concepts to transition economies or emerging markets. Indeed, empirical analysis shows that the benefits of equity markets vary across industries and across countries at different stages in their economic development. Capital-intensive industries, which characterize countries in their earlier development stages, benefit more from credit financing, which typically goes hand in hand with concentrated ownership.³⁵ Industries in research and development, by contrast, correlate with well-developed capital markets. It is therefore possible that given their current state of economic development, transition economies may benefit from a relatively concentrated ownership structure. Indeed, data for the Czech Republic lend support for this proposition.³⁶

Company groups differ from ownership concentration in several respects. It is meaningful to talk about a company group only for 'a cluster of several, typically legally independent firms'.³⁷ Moreover, whereas ownership concentration clearly refers to equity ties between companies, company groups may consist of

³² See Daniels and Iacobucci, 'Some of the Causes and Consequences of Corporate Ownership Concentration in Canada', in: Morck (ed.), *Concentrated Corporate Ownership* (Chicago 2000) 81 at p. 83 for a useful summary of this argument.

³³ See in particular Shleifer and Vishny, 'A Survey of Corporate Governance', 52 *The Journal of Finance* (1997) 737 and the studies by La Porta et al., *supra* n. 5.

³⁴ Hansmann and Kraakman, *supra* n. 3.

³⁵ See Carlin and Mayer, 'Finance, Investment and Growth', available on <www.ssrn.com> (viewed 2000).

³⁶ Claessens and Djankov, 'Ownership Concentration and Corporate Performance in the Czech Republic', 27 *Journal of Comparative Economics* (1999) 498. The analysis is based on 1,782 firms listed on the Prague stock exchange. Performance indicators used are accounting data, including profitability and labor productivity. Note that this result may be driven by the fact that many blockholders are foreign strategic investors. Thus, firms may benefit not only from better corporate governance, but also greater access to capital and managerial expertise. See also *id.* at p. 507.

³⁷ See Granovetter, 'Business Groups', in: Smelser and Swedberg (eds.), *The Handbook of Economic Sociology* (Princeton, N.J. 1994) 453 for this definition.

equity as well as contractual relations.³⁸ For our purposes, we define a company group as a cluster of legally independent companies that are linked by formal ties, be they contract or equity, and that are subject to the same management strategy set typically by the leading company in the group. Using this definition as a basis, the following sections review theories from an institutional economics perspective on the rationale for company groups. Economic theories were long preoccupied with exchange relations on markets. Only with Ronald Coase's famous article published in 1937³⁹ has the firm received greater attention. Coase posed the crucial question why firms exist, i.e., why not all transactions that make up the production process are conducted on markets through contracts rather than through property rights and the internal organization of a firm. His answer was that the market mechanism has its own costs. The suppression of the price mechanism within the firm and its substitution with central administration may substantially reduce transaction costs.⁴⁰

Roughly sixty years later, Granovetter has extended this question and has asked why company groups exist, how they evolve, and what function they perform in different economies.⁴¹ He reviews studies of company groups around the world, which show that in many countries it is not the individual firm that dominates, but a group of more or less formally organized companies of various sizes. Examples include the *keiretsu* in Japan, the *chaebol* in Korea, the various family groups, such as the *Tata*, in India, or the *grupos económicos* in Latin America. In Western countries, apart from the German concern structures, the family based company groups in Sweden (Wallenberg family), but also the company groups in France and Belgium, whose emergence at least in part can be traced to state intervention, deserve special mention.⁴²

Institutional economics and its sub-specialty, transaction cost economics, view company groups primarily as a response to imperfect markets and weak institutions. Underdeveloped capital markets, insufficient information transparency or a weak legal framework create incentives for firms to either form new or join existing groups.⁴³ The causes for their emergence also explain their function: they buffer financial problems and liquidity crises of individual firms and improve access by firms to capital markets by, for example, the reciprocal provision of securities and guarantees among group members. Government

³⁸ Some authors would also include informal ties, such as kinship relations. See *ibid.*

³⁹ Coase, 'The Nature of the Firm', *Economica* (1937) 386.

⁴⁰ See also Williamson, *Markets and Hierarchies, Analysis and Antitrust Implications: A Study in the Economics of Internal Organization* (New York 1975); for a summary of the key arguments relevant for the theory of the firm see Williamson, 'Transaction-Cost Economics: The Governance of Contractual Relations', 22 *Journal of Law and Economics* (1979) 233.

⁴¹ See Granovetter, *supra* n. 37.

⁴² Wymeersch, *Groups of Companies in the EEC* (Berlin/New York 1993).

⁴³ See in particular Kali, 'Endogenous Business Groups', 15 *The Journal of Law, Economics and Organization* (1999) 615 for this view of company groups.

intervention is an alternative explanation for company groups. Tax considerations weigh heavily not only in the choice of legal forms, but also on the design of intra-firm relations. To avoid such distorting effects, legislatures should be weary of creating market-distorting incentives.⁴⁴

Membership in company groups can be advantageous both *vis-à-vis* an isolated firm as well as *vis-à-vis* a fully integrated firm.⁴⁵ Company groups offer advantages over independent firms, if the transaction costs of market relations exceed the costs of co-ordinating activities among members of the group. Groups may also be superior to full integration, because legal independence of group members facilitates the delegation of activities and decision-making. This is relevant in particular for heterogeneous activities or highly independent stages of the production process. The establishment of company groups may lead to financial advantages for the leading company in the group, but also for other members. One reason is that the formation of a group may result in the concentration of economic power, thus reducing competition and allowing the group to reap the benefits of monopoly rents. Another is that companies may participate in the profits generated by other member firms either through equity stakes or contractual arrangements that transfer part of the profits to the leading firm. At the same time, they may reduce their own liability arising out of tort (including product liability) or contract, as formally each group member remains legally responsible for its own obligations. The diversification of risks and liability means that the group functions as a buffer against negative economic externalities, although this may come at the expense of an individual member. Another source of financial benefits is that members may benefit from lower costs of external finance that is provided by other group members. A classic example is the establishment of pyramid structures. An alternative to this structure is the inclusion of an external financier (for example a bank) that holds a minority stake in the parent company, or co-owns a joint company and facilitates access to funds in the form of long-term credits, leasing or rent arrangements. Finally, group members can provide each other with securities and guarantees in order to obtain credits from external sources.

As this summary reveals, the field of institutional economics is primarily concerned with market distortions as determinants for the formation of company groups. Absent high information and other transaction costs, there should be no reason for the emergence of groups. From this analysis follows that the

⁴⁴ The expected sell off of large equity stakes by German banks and other companies in response to the expected change in tax law is ample evidence of the impact of tax considerations on the ownership structure of enterprises. See 'Germany's Quiet Tax Reform', *The Wall Street Journal*, 28 December 1999, A 18:1.

⁴⁵ For a detailed analysis of the economic rational of company groups see Kalfass, 'Ökonomische Analyse der Konzernbildung', in: Mestmäcker and Behrens (eds.), *Das Gesellschaftsrecht der Konzerne im internationalen Vergleich* (Baden-Baden 1991). The subsequent analysis draws heavily on his work.

primary purpose of regulatory intervention should be the reduction of transaction costs, i.e., by improving access to information through disclosure requirements, strengthening institutions like courts that facilitate contract enforcement, and antitrust measures that enhance the competitiveness of markets.⁴⁶

B. Application to transition economies

In the context of transition economies, these remedies appear to be most appropriate for company groups that emerged in the post-socialist period, especially the network restructuring groups.⁴⁷ These groups emerged in response to transaction cost problems faced by individual firms. It is therefore plausible that improvements in law and legal institutions, i.e., a reduction in transaction costs, would lead to a reversal of this process. The same remedies may work in the case of groups that resulted from a particular privatization strategy (privatization groups). They may dissolve themselves in light of potential efficiency gains. In contrast to network restructuring as well as privatization groups, oligarch groups are not as likely to respond to incentives, as their primary benefit results from the political benefits of economic power. With respect to company groups that are a legacy either of the classic socialist regime or the socialist reform period, the implications are also less certain. Classic socialist groups were created by political fiat. Their organizational and management structure was not designed according to economic efficiency criteria. Those who control these groups, in particular top management and their affiliates in the state bureaucracy (including in the post-socialist privatization or state property management agencies), may have little interest in undermining their own future by dissolving these groups.

The choice of reform strategies should therefore be informed by the legacy of company groups and the political economy in different transition economies. Changing the incentive structures of firms may not be sufficient, if the formation of groups is motivated by either political factors or is a defense mechanism against market based reforms.

Even where these reform strategies may work in principle (i.e., for network restructuring or privatization groups), it should be noted that this process will take time. Institutions for a market economy are not created over night, as the experience of the past ten years of transition amply demonstrates. In the meantime, the existence of company groups may be a desirable alternative. Absent adequate market institutions they can be viewed as transaction enabling.⁴⁸ The

⁴⁶ This is the policy implication that Kali draws from his analysis of company groups. See Kali, *supra* n. 43.

⁴⁷ Compare the typology of company groups we developed *supra* II.

⁴⁸ See also Khanna, *supra* n. 29.

longer this process lasts, the less likely it is that it can be easily reversed. Path dependence theory suggests that even if alternative strategies become more efficient over time, switching costs may be too high to implement change.⁴⁹

Where this is the case, more proactive policies, for example in the form of competition policy, may be necessary.

To justify such an intervention we must return to the question of the costs and benefits of company groups. To the extent they are transaction enabling, because they substitute for underdeveloped markets and weak legal institutions, the benefits seem to outweigh the costs. Company groups may, however, have a negative impact on the competitiveness of an economy. The greater security group membership affords firms may also make them less responsive to changing market conditions. The struggle of the Korean *chaebol* since the 1997/98 Asian financial crisis gives ample evidence of the adaptation costs of enterprise structures that relied too long on group protection.⁵⁰ In addition, they create conflicts of interest between investors of individual members and the group at large.⁵¹ The irony is that group membership may be a *conditio sine qua non* for the survival of many companies during the transition process, but continuing dependence on group membership under changing market conditions may undermine the competitiveness of the same firms in the long term. The challenge for policy-makers is therefore to balance the short-term benefits with the potential long-term costs of company groups.

IV. Legal regulation of company groups

Company groups have received much greater attention in legal literature as well as in legislation, in particular in Continental European legislation.⁵² Within the

⁴⁹ North, *Institutions, Institutional Change, and Economic Performance* (Cambridge/New York 1990) for a basic exposition of the path dependency theory and Roe, 'Chaos and Evolution in Law and Economics', 109 *Harvard Law Review* (1996) 641 for its application to legal evolution.

⁵⁰ On the fall-out of the Asian financial crisis on the enterprise sector in Asia compare Rajan and Zingales, *Which Capitalism? Lessons from the East Asian Crisis*, Working Paper, Chicago University (1998).

⁵¹ See also Khanna and Palepu, 'Is Group Affiliation Profitable in Emerging Markets? An Analysis of Diversified Indian Business Groups', 55 *Journal of Finance* (2000) 867. Based on their analysis of company groups in India, however, they conclude that overall affiliation with highly diversified groups has a positive impact on affiliates.

⁵² There is a huge amount of literature on company groups (concerns) in Germany. See the references in Emmerich and Sonnenschein, *Konzernrecht*, 7th ed. (Munich 2001). We focus here only on comparative studies. See, for example, Mestmäcker and Behrens (eds.), *supra* n. 45, Schmitthoff and Wooldridge (eds.), *Groups of Companies* (London 1991), Wymeersch (ed.), *Groups of Companies in the EEC* (Berlin/New York, 1993), Lutter (ed.), *Konzernrecht im Ausland* (Berlin 1994), and most recently Forum Europaeum Konzernrecht, 'Konzernrecht für Europa' [Corporate Group Law for Europe], *Zeitschrift für Unternehmens- und Gesell-*

EU, a comprehensive regulation of company groups exists in Germany since 1965 as well as in Portugal. Many other countries have legislation on company groups in specific areas of the law, e.g., in tax law, banking supervision, and group accounting law. There is also a substantial body of case law on groups in most jurisdictions, reflecting the fact that company groups are an important real world phenomenon. Furthermore, attempts to develop principles for common group law (beyond the already existing European group accounting law) in the EU are currently under way.⁵³

Transition economies have followed different strategies in developing a legal framework for company groups. Some have imported the German *Konzernrecht* wholesale. This is the case in Croatia, the Czech Republic and Slovenia. Others, such as Hungary, have been more selective, and have adopted only a few provisions, in particular those that appeared relevant for dealing with the phenomenon of transnational groups. Yet others, foremost among them Poland, have been reluctant to enact specific legislation on company groups and have instead adopted a policy of 'wait and see and pick and choose'.⁵⁴

Even where a comprehensive group law does not exist, there are many other ways for a legal system to address the phenomenon of company groups. One approach is to treat the relation among group members as parent-subsidiary relations and deal with liability issues and shareholder rights under the rubric of blockholders. Creditor protection is achieved by way of piercing the corporate veil, the doctrine of equitable subordination and fraudulent conveyance law.

schaftsrecht (1998) 672. For the English language version of the principles developed by the Forum Europaeum see 1 *EBOR* (2000) 165.

⁵³ Detailed propositions have already been developed by a group of legal experts from different European countries. See Forum Europaeum, *supra* n. 52. For a critical assessment of these propositions, see Fleischer, 'Neue Entwicklungen im englischen Konzernrecht, Vergleichende Notizen im Lichte der Empfehlungen des Forum Europaeum Konzernrecht', *Die Aktiengesellschaft* (1999) 350; Kluver, 'European and Australian proposals for corporate group law: a comparative analysis', 1 *EBOR* (2000) 287; Schön, 'Das Bild des Gesellschafters im Europäischen Gesellschaftsrecht' [The Concept of the Shareholder in European Law], *Rabels Zeitschrift* (2000) 1, English language version: 1 *EBOR* (2000) 3; Windbichler, 'Corporate Group Law for Europe: Comments on the Forum Europaeum's Principles and Proposals for a European Corporate Group Law', 1 *EBOR* (2000) 265. As to the reception of these proposals by the international legal community see Hopt, 'Konzernrecht für Europa – Zur Diskussion um die Vorschläge des Forum Europaeum Konzernrecht' in: Basedow, Drobnig, Ellger, Hopt, Kötz, Kulms and Mestmäcker (eds.), *Aufbruch nach Europa, 75 Jahre Max-Planck-Institut für Privatrecht*, Tübingen 2001, p. 17. The proposals have been discussed also in Japan and have been translated into Japanese. Some of the proposals of the Forum Europaeum have been adopted by the High Level Group of Company Law Experts in its first and second reports to the European Commission of January and October 2002. The recommendations as to the mandatory bid, the squeeze-out and the sell-out have been taken up by the European Commission in its draft 13th directive as of October 2, 2002, COM (2002) 534 final.

⁵⁴ For details see Jessel-Holst, in this volume pp. 43.

This approach has been taken by the United States.⁵⁵ Another approach, used often cumulatively, is to deal with company groups from the perspective of antitrust law. It deals with behavior of economic actors (and economic structures) that may adversely affect competition. A wide interpretation of such behavior may imply that strong ties between legally independent firms may be deemed anti-competitive and thus illegal. In particular the early development of antitrust law in the United States can be described as a process that forced firms to choose between full vertical integration on the one hand, or arms length relationships on the other.⁵⁶ To put it simply, antitrust law may be characterized as the law that establishes the limits of firm co-operation, while group law deals with the protection of stakeholder interests within groups. In the following sections we sketch out important control mechanisms for company groups in both areas of the law with emphasis on those mechanisms that may be relevant for transition economies. We do not attempt to offer a comprehensive analysis of either body of law.

A. Competition law

The function of competition law is to ensure the competitiveness of markets, this being an important goal of the transition process. The initial conditions as well as the circumstances of the transition process have demonstrated that this is a difficult and long-term process.⁵⁷ Its success depends to a large extent on the ability of these countries to build effective market institutions, in particular courts and antitrust agencies whose task is to watch over the observation of the rules of the game. They need to carefully manage the transition process between the Skylla of excessive concentration of economic power in response to adverse market conditions, and the Charybdis of excessive regulation. The

⁵⁵ Clark, *Corporate Law* (Boston/Toronto, 1986) ch. 2 (duties to creditors), ch. 7.8 (parents and subsidiaries), ch. 10 et seq.; Brudney and Clark, 'A New Look at Corporate Opportunities', 94 *Harvard Law Review* (1981) 1044. Blumberg has made substantial efforts to develop principles of group law for American law, but they have not found widespread acceptance. Blumberg, *The Law of Corporate Groups* (Boston 1987). Cf. the survey by Blumberg, 'The Increasing Recognition of Enterprise Principles', 28 *Connecticut Law Review* (1996) 296.

⁵⁶ For a detailed analysis of the relation between corporate and antitrust law in the US and its impact on the development of the corporate sector, see Hovenkamp, *Enterprise and American Law, 1836-1937* (Cambridge, Mass, 1991). For an analysis of the relation between merger waves and changes in antitrust law, see Kovacic, 'Failed Expectations: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration', 74 *Iowa Law Review* (1989) 1105.

⁵⁷ See Commander, Dutz and Stern, 'Restructuring in Transition Economies: Ownership, Competition and Regulation', *Proceedings of the Annual Bank Conference on Development Economics* (Washington, D.C. 1999) for an assessment of the competitiveness of markets in transition economies. See also EBRD, *Transition report - Ten years of transition* (London 1999) ch. 7.

latter might dwarf economic activities, if market transactions are too costly and regulation prevents the internalization of transaction costs by forming groups.

In most countries, transition countries as well as others, the national jurisdiction has become too narrow to deal with issues of competitiveness. Markets are becoming increasingly international thereby challenging the national boundaries of regulation. The bundling of national antitrust laws at the European level is a reaction to this development, but appears not to be sufficient in an era of globalization. The smaller countries of Central and Eastern Europe are strongly affected by this process. In fact, as the – admittedly limited – data we present in the Appendix suggest, transnational groups are a far more important factor in these countries than purely domestic groups.

The most important regulatory tools to deal with group related issues are the prohibition of cartels, merger control, and intervention when firms exploit their market dominant position.⁵⁸ The appropriateness of these tools, the criteria used to define a restraint on competition, and the theoretical assumptions on which they rest is subject to considerable and ongoing debate. Whatever the merits of this debate, those transition economies that are in the process of joining the European Union have relatively little choice over the tools and concepts for their future competition policy, which is set in Brussels, not in Warsaw, Prague, or Budapest. In fact most countries, including second tier accession countries have designed and reformed their competition laws already in the shadow of European competition regulations.⁵⁹ While the existing regulatory framework may not be a perfect match for new Member States, opting out of this framework raises substantial political as well as economic costs, which may not be worth the effort. In fact, the very existence of a developed and thus predictable legal framework for competition law may facilitate rather than hinder the reform process.⁶⁰

This still leaves open the question as to how rigidly these regulations should be applied to transition economies, and whether temporary exemptions should be made for specific sectors. This could be justified by the old infant industry argument, namely that countries should be given the time to nurture and grow their domestic companies before exposing them to the rules of international competition. Apart from the fact that infant industry protection strategies have rarely been successful, the factual situation in transition economies is quite different. They inherited a highly concentrated industry structure from the socialist system, which tends to crowd out small and medium size enterprises. Still, an extensive, rigidly enforced merger control without any exemptions might also be undesirable in economies where mergers perform an important

⁵⁸ For a detailed account of these tools, compare Dreher, in this volume pp. 145.

⁵⁹ *Ibid.*

⁶⁰ A similar point was made by Fornalczyk at the symposium.

function in the process of 'secondary privatization'.⁶¹ This concept refers to the reallocation of property rights subsequent to privatization. Since privatization programs could not assure that those who would use the assets most productively would obtain control right away, the subsequent sale of assets was widely regarded as a crucial part in reforming the ownership structure of firms.

In addition, the market for control could play a potentially useful role as a corporate governance device.⁶² Regulatory intervention, e.g., by a mandatory bid provision coming in at too low a participation level, may make such transactions too costly, and, even though well-intended, may therefore have adverse consequences. Yet, regulatory supervision could also function as a check on the extent to which companies choose group membership as a defense strategy against corporate control mechanisms and the force of competition. This may be a case for prohibiting managers of target companies from frustrating action in case of a takeover.⁶³ Proponents of the equivalent of the infant industry argument in the market for corporate control would argue that requiring neutrality may expose domestic companies to foreign takeovers at a time when a level playing field has not been established yet. In fact, this argument is frequently made to protect European firms from takeovers by American companies. If one assumes that takeovers are usually efficiency enhancing, this argument is not convincing as companies and ultimately the economy would benefit from the change in ownership and new inputs of capital and expertise. If, by contrast, takeovers are part of a strategy to ensure market control and eliminate competition, one cannot deny some merit to this argument. In transition economies (as elsewhere), there is evidence for both scenarios. Until stronger evidence makes

⁶¹ For a similar argument see Soltysinski, 'Transfer of Legal Systems as Seen by the "Import Countries": A View from Warsaw', in: Drobniak, Hopt, Kötz, Mestmäcker et al. (eds.), *Systemtransformation in Mittel- und Osteuropa und ihre Folgen für Banken, Börsen und Kreditsicherheiten* (Tübingen 1998) 69. Cf. also § 37 (3) of the German Anticartel Act 1998. This provision exempts financial intermediaries from merger control if they do not vote their shares and resell them within one year.

⁶² On takeover transactions as a control device and their impact on management behavior, see Coffee, 'Shareholders Versus Managers: The Strain in the Corporate Web', in: Lowenstein and Ackerman (eds.), *Knights, Raiders and Targets, The Impact of the Hostile Takeover* (Oxford 1988); Romano, 'A Guide to Takeovers: Theory, Evidence, and Regulation', 9 *Yale Journal on Regulation* (1992) 119, also in Hopt and Wymeersch (eds.), *European Takeovers* (London 1992) 3. Cf. also Hopt, Kanda, Roe, Wymeersch and Prigge (eds.), *Comparative Corporate Governance* (Oxford 1998) ch. 8.

⁶³ Cf. Mühlert, 'In Defense of Passivity – on the Proper Role of a Target's Management in Response to a Hostile Tender Offer', 1 *EBOR* (2000) 445. The Thirteenth EU Directive (see *infra* n. 78) contains such a rule; cf. Hopt, 'The Duties of the Directors of the Target Company in Hostile Takeovers – German and European Perspectives', in: Ferrarini, Hopt and Wymeersch (eds.), *Capital Markets in the Age of the Euro* (The Hague: Kluwer International 2002) 391. See also Bebchuk and Ferrel, 'Federalism and Corporate Law: The Race to Protect Managers from Takeovers', 99 *Columbia Law Review* (1999) 1168.