European Community Company and Securities Law: A Canadian Perspective

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The author suggests that a systematic and contextual understanding of European Community ("E.C.") company and securities law is required if Canadian businesses and investors are to profit from the rapidly changing social, economic and political structures of Europe. Law reformers, as well, can take from the E.C. many relevant and potentially revealing comparisons if the context of the development of E.C. company and securities law is properly understood. Accordingly, the author presents a systematic survey of E.C. law beginning with the E.C.'s institutional structure. The state of the E.C.'s company and securities law is the explored, followed by an analysis of its central themes and issues of special interest to the Canadian business, investment and law reform communities, such as issues of employer participation and corporate groups.

L'auteur suggère qu'une compréhension systématique et contextuelle du droit de la Communauté économique européenne ("C.E.E.") en matière de compagnies et valeurs mobilières est nécessaire si les entreprises et investisseurs canadiens doivent profiter des structures sociales, économiques et politiques, en évolution rapide, de l'Europe. Les spécialistes de la réforme du droit peuvent aussi trouver dans le cadre de la C.E.E. plusieurs comparaisons pertinentes et potentiellement révélatrices, si le contexte du droit de la C.E.E. en matière de compagnies et de valeurs mobilières est correctement compris. En conséquence, l'auteur présente un aperçu systématique du droit de la C.E.E. à partir de la structure institutionnelle de la C.E.E. Puis, l'état du droit de la C.E.E. en matière de compagnies et de valeurs mobilières est exploré ; ce à quoi fait suite une analyse de ses thèmes centraux et des questions d'intérêt particulier aux mondes canadiens de l'entreprise, de l'investissement et de la réforme du droit, telles la participation des employés et les groupes corporatifs.

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Introduction

Developments in the European Community (E.C.) are rapidly changing the social, economic and political structure of Europe. Many argue that because of this Canadians need to be better informed about the E.C. The media have responded to a certain extent. Unfortunately, however, those who want to investigate E.C. legal issues from a Canadian perspective will discover significant gaps in the literature.

E.C. company and securities law is one area which has not been examined systematically from a Canadian perspective. This gap is unfortunate since Canadian businesses, investors and law reformers all have good reasons to examine E.C. company and securities law. In terms of Canadian business, government officials and the financial press have heralded the commercial opportunities a single E.C. market will afford. The Canadian business community has responded cautiously thus far, but Canadian companies now appear ready to increase their involvement in Europe. If they attempt to penetrate the European market by establishing a branch or subsidiary in the E.C., they will have to confront and understand the Community's company law measures.


3The best example is a book by an associate editor of The Financial Post, G. Pitts, supra, note 2. See also the articles cited in note 2, supra, and “Post-'92 Europe Lures Investors” The Financial Post (14 November 1988) 35 [hereinafter “Post-'92”; and “RRSP Fund Looks to Europe for Growth” The Financial Post (11 May 1990) 16 [hereinafter “RRSP”]. Furthermore, on March 12th and 13th, 1990 the Canadian Broadcasting Corporation program, The Journal, broadcast a segment entitled “Europe Unbound.”


Canadian investors are also becoming increasingly aware of the E.C.'s efforts to create a single market within the Community. Consequently, they are becoming more interested in buying shares in European companies. Since there is a reasonable prospect that E.C. company and securities law will have an impact on the share values of E.C. companies, Canadian investors would be well advised to monitor developments in this area.

Canadian law reformers also have good reason to examine E.C. company and securities law. There are important similarities between the E.C. and Canada which make comparisons relevant and potentially revealing. This is illustrated by the fact that Canadian academics have examined a number of E.C. company law topics and in so doing have made useful and pertinent observations about Canadian law.

The work which has been done by Canadians on E.C. company and securities law no doubt is useful to Canadian businesses, investors and law reformers. Still, these groups will find it difficult to gain a complete appreciation of the topic on the basis of what Canadians have written. This is because no Canadian commentator has provided an overview of E.C. company and securities law or has placed the topic in its institutional, economic and social contexts.

This article attempts to provide a systematic survey of E.C. company and securities law for a Canadian audience. The article is divided into four parts. The first discusses the E.C.'s institutional structure. The second summarises the present status of the E.C.'s company and securities law measures. The third explores the central themes of E.C. company and securities law. The fourth analyzes issues of particular relevance to Canadian businesses, investors and law reformers. The article concludes with some observations about how Canadians should examine European Community legal issues.

I. Institutional Overview

The E.C.'s institutional and jurisdictional structure has recently been examined elsewhere from a Canadian perspective. Consequently, no attempt will be made here to outline this topic in detail. Nevertheless, some basic concepts need

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6Interest in the E.C. is reflected by the Europe 1992 Fund, which the Chevron Fund Management Ltd. formed in 1989 to invest in companies expected to benefit from the single market project. See Pitts, supra, note 2 at 72; "Post-'92," supra, note 3, and "RRSP," supra, note 3.


8See supra, note 4.
to be kept in mind to understand the present status of E.C. company and securities measures.

The European Community is made up of twelve member states. The E.C. operates as a supranational body, which makes it a unique organisation in international law. For example, unlike conventional international organisations, the E.C. can create rights and duties for individuals without the intervention of national parliaments. Moreover, E.C. law prevails over the law of its members in the event of a conflict.

The E.C.’s cornerstone is the Treaty of Rome, which was signed in 1957. The Treaty sets out the Community’s essential objectives, which include establishing a common market and integrating the member states’ economic policies. It also creates an institutional structure to facilitate the achievement of these objectives.

Three of the institutions created by the Treaty play a key role in the development of Community legislation. These are the European Commission, which is the central bureaucratic component of the Community; the European Parliament, which is primarily a consultative rather than legislative body; and the Council of Ministers, which has ultimate legislative authority in the E.C.

The European Commission commences the legislative process by making a proposal. This is consistent with its formal role under the Treaty of Rome, which is to initiate the legislative process and to ensure that Treaty provisions are observed. The Commission also often participates in other stages of the decision-making process, such as legislative debate and the implementation of E.C. measures by member states.

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9 They are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain and the United Kingdom.


12The Treaty says these objectives need to be fulfilled to foster the harmonious development of economic activities among the E.C.’s member states, to improve economic conditions and to promote closer relations between E.C. members — supra, art. 2.


14 Owen & Dynes, supra, note 1 at 36. See generally Treaty of Rome, arts 155-63, as amended by the Treaty Establishing a Single Council and a Single Commission of the European Commu-
The Commission submits its legislative proposals to the Council, which is composed of member state representatives who are usually ministers in their respective national governments. A proposal will then follow one of two routes, depending on its legislative basis. Under either route, the Council must consult with the European Parliament, which consists of representatives directly elected in the member states. The extent of the Parliament's participation and the level of support needed for Council approval differs depending on which route the legislation is following. Ultimately, however, both procedures conclude with Council consideration of the measure. If the Council adopts a proposal, it attains legislative force.

The Commission, the Parliament and the Council do not have an open-ended jurisdiction to enact Community law. The Treaty of Rome allocates specific legislative and administrative powers to the E.C. measures which exceed the Community's jurisdiction may be struck down by the European Court of Justice. The Court, which has a number of other important adjudicatory functions, has itself played an important role in the development of Community law. E.C. legislative and administrative actions can take a variety of forms. Two of the most important are directives and regulations. Directives are addressed to the member states and require their governments to enact legislation consistent with the relevant E.C. policy. Generally speaking, directives themselves do not create rights that can be directly enforced by individuals in
national courts. The European Court, however, has created some important exceptions.\(^9\)

The Community generally gives member states a substantial amount of time to implement directives. Once the grace period expires, member states which have not complied with a directive can be sanctioned by the European Court of Justice.\(^2\)

Regulations, unlike directives, do not need to be implemented by the member states. Instead, they have immediate legal effect.\(^2\) Consequently, regulations may pre-empt national legislative competence in the areas they cover, national courts must take judicial notice of regulations and individuals can directly enforce certain provisions in regulations.\(^2\)

II. Overview of European Community Company and Securities Law

The E.C.'s company and securities law measures are divided into three basic groups. The first group is made up of measures which deal directly with company law. The second is composed of securities law measures. The third is made up of E.C. legislative provisions which are not company and securities law measures \textit{per se}, but which have an important impact on these areas.

A. Company Law Measures

There are thirteen E.C. company law directives. Seven of the company law directives have been approved by Council and presently require the member states to enact implementing legislation. These are the First, Second, Third, Fourth, Sixth, Seventh and Eighth Directives.\(^2\) The First Directive instructs the member states to require all companies to file prescribed information with a public registry. The Second Directive governs the formation of public companies and regulates share capital. The Third Directive deals with mergers between companies within the same member state. The Sixth Directive seeks to


\(^{20}\)See \textit{Treaty of Rome}, art. 169.


\(^{22}\)Wyatt & Dashwood, \textit{ibid.} at 38-41.

harmonise member state legislation governing transactions in which public companies are divided up by the sale of their assets. The *Fourth, Seventh* and *Eighth Directives* are interrelated. They regulate accounting standards for individual companies and company groups and establish qualification and independence standards for auditors.

Two other company law directives have been approved by the Council but do not yet require member state implementation because the grace period for doing so has not expired. One is the *Eleventh Company Law Directive*, which regulates disclosure by company branches when the company is registered in a non-E.C. country or a different member state than the branch.\(^{24}\) The second is the *Twelfth Directive*, which requires member states to allow the formation of one-person companies.\(^{25}\) At present, member states must implement the *Twelfth Directive* by January 1992 and the *Eleventh Directive* by January 1993.\(^{26}\)

Three draft company law directives have been submitted by the Commission but have not yet been formally considered by the Council. These are the *Fifth Directive*, which deals with the structure and management of public companies, the *Tenth Directive*, which applies to mergers between public companies located in different member states and the *Thirteenth Directive*, which regulates the conduct of takeover bids.\(^{27}\)

One company law directive has never been formally submitted by the Commission to other E.C. institutions. This is the *Ninth Directive*, which deals with corporate groups. The Commission circulated a draft proposal of this *Directive* in the early 1980s, but did not proceed further because of the hostile reception the draft received.\(^{28}\) Still, the *Ninth Directive* remains on the Commission's agenda.

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\(^{26}\) ibid., art. 8, and supra, note 24, art. 16.


\(^{28}\) Again, because the Commission never submitted the *Ninth Directive* to the Council, it has not been published in the Official Journal. On the contents of the draft, see infra, note 115 and accompanying text.
The Commission has also formally proposed to the Council that the Community enact a European Company Statute. The Statute would provide companies with internal legal rules that are independent of member state law. The Commission first proposed a European Company Statute in 1970 and submitted its latest draft to the Council in 1989. The Commission has suggested that the Statute take the form of a regulation rather than a directive.

B. Securities Law

Four securities law directives are presently binding on the member states. Three deal with companies listed on the stock exchanges in the various member states. These are the Admissions Directive, the Listing Particulars Directive and the Interim Reports Directive. Together these directives regulate disclosure by companies to stock exchanges and to the public. They require disclosure to take place prior to listing and at prescribed instances thereafter. The fourth measure, the Public Offer Prospectus Directive, extends many of the disclosure requirements to all companies making a public offering of securities.

One securities law directive has been approved by the Council but does not yet require implementation. This is the Insider Trading Directive, which

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instructs member states to pass legislation prohibiting insider dealing. The member states must implement the Directive by June 1, 1992.32

C. Related Measures

There are some E.C. measures which do not directly deal with company and securities law but which merit special attention because of the impact they may have on the operations of Community companies. One was enacted by the Community in 1985. This is the European Economic Interest Grouping (E.E.I.G.) Regulation, which allows member state businesses to jointly pursue certain economic activities.33

Another non-company law measure which merits comment is the Vredeling Directive,34 which has only been formally proposed by the Commission. This Directive takes its name from Hank Vredeling, who was the Social Affairs Commissioner at the Commission when that body first proposed the measure in 1980. Its essential objective is to ensure that parent companies keep employees in subsidiary companies informed about group affairs.

Though the Vredeling Directive formally remains a valid Commission proposal to the Council, due to political controversy it has not been debated seriously in the Community since the mid-1980s. The Commission, however, has not given up on the basic concept. Indeed, the Commission will probably propose to the Council a similar, though more moderate, measure in the near future.35

III. Central Themes of European Community Company and Securities Law

A. How Much Co-Ordination Should There Be Between Member State Laws?

The Treaty of Rome’s drafters clearly contemplated that Community institutions would engage in company law reform because art. 54(3)(g) expressly gives the Community the jurisdiction to enact company law directives.36 This

36Supra, note 11.
article requires the Council and the Commission to co-ordinate member state laws to protect shareholders and others dealing with companies. It is the Treaty provision upon which most company law directives have been based.\textsuperscript{37}

Community institutions have yet to adopt a consistent, coherent approach to the co-ordination of company and securities law. The E.C. has never attempted to develop uniform legal rules in the area.\textsuperscript{38} Other than agreeing that uniformity is not the ultimate objective, however, Community institutions have never been able to determine definitively what degree of co-ordination there should be.\textsuperscript{39}

Until the mid-1980s, E.C. officials, especially in the Commission, generally wanted to use E.C. company and securities law measures to eliminate as many differences as possible in member state legislation. The terminology which was most often used to describe this approach was the harmonisation of company and securities law. Part of the reason Commission officials favoured harmonisation was political. They assumed that the development of similar legal rules throughout the E.C. would help to advance the cause of centralisation and would foster the development of the Community.\textsuperscript{40}

The possibility that E.C. companies might rely on guarantees of freedom of establishment in the Treaty of Rome to migrate from regulatory to liberal jurisdictions also contributed to the emphasis on harmonisation. Member states with strict company laws were concerned that their companies would use Treaty of Rome principles to reincorporate in member states with less stringent regimes. The concern was a legitimate one. Anecdotal evidence suggests that businesses in the E.C. will make efforts to adopt the legal structure which imposes the least costs on them.\textsuperscript{41} For example, many German firms choose

\textsuperscript{37}Encyclopedia, supra, note 11, para. B10-127.


\textsuperscript{41}In D.H.M. Segers v. Bestuur Van de Bedrijfsvereniging Voor Bank-En Verzekeringswezen [1987] 2 C.M.L.R. 247 (E. Ct. J.) Segers, a Dutch national, ran a commercial undertaking which had its registered office in the Netherlands. He chose to incorporate his business under British law instead of Dutch law because the waiting period for incorporation was shorter and because the designation "Ltd." was more attractive than the Dutch equivalent, "BV."
their business form to evade German legislative requirements concerning information disclosure, minimum share capital and employee representation on boards.\textsuperscript{42}

The concern about migration has a strong historical tradition in the Community. In Great Britain, Ireland and the Netherlands, as in Canada, the internal affairs of companies are governed by the jurisdiction of incorporation.\textsuperscript{43} This allows corporate participants substantial choice about the company law rules that apply to their firm. On the other hand, in the other nine member states, internal affairs are governed by the law of the country where a company has its real seat, which essentially is its centre of operations. Courts developed this real seat doctrine to curtail nationals from obtaining competitive advantages by incorporating elsewhere under a more liberal company law regime.\textsuperscript{44} The result is that in most member states companies which do not incorporate where their real seat is located risk being treated as non-entities or having their internal affairs governed by the company law of the real seat’s member state.

Concerns about the migration problem coincided neatly with the Commission’s favourable view towards centralisation. Commission officials argued that harmonising member state company legislation would eliminate the possibility of migration since companies would have no incentive to change jurisdictions.\textsuperscript{45}

\textsuperscript{42}E.g., some German businesses restructure to avoid the substantial management rights given to employees under the 1976 Co-Determination Act and choose the less regulated private company (Gesellschaft mit beschränkter Haftung, or GmbH) form over the public company (Aktiengesellschaft, or AG). Other German firms evade the Co-Determination Act and other regulatory requirements by forming a company in Britain. They then operate in Germany with a branch or do business as a limited partnership (Kommanditgesellschaft, or KG), with the British company as the only general partner. See Buxbaum & Hopt, supra, note 18 at 171, 185 & 187; W.F. Ebke, “The Limited Partnership and Transnational Combinations of Business Forms: ‘Delaware Syndrome’ Versus European Community Law” (1988) 22 Int. Lawyer 191 at 194-95; B.A. Streeter III, “Co-Determination in West Germany — Through the Best (and Worst) of Times” (1982) 58 Chi. Kent L. Rev. 981 at 998-99, and G.H.W. Stratmann, “Partnerships Versus Corporations: Why and When to Use Partnerships in the Light of Legal Format and Tax Treatment” (1980) 8 Int. Bus. Lawyer 317.


\textsuperscript{44}On the real seat rule and its history, see Buxbaum & Hopt, ibid. at 68-70; Stein, ibid. at 29-32 & 399-401, and J. Dine, “The Harmonisation of Company Law in the EC” 1990 Yearbook of European Law [forthcoming].

A necessary corollary of harmonisation, of course, was substantial E.C. control over company and securities law.

Eliminating differences between member state company laws required the E.C. to enact very detailed directives. This is because specific instructions were needed to address all significant differences between member state company laws and to ensure that the implementing legislation in each country was similar in all material respects. Commission officials ran into political problems, however, when they proposed directives prepared along these lines. Many member states turned out to be concerned about a loss of sovereignty and about protecting favoured company law principles. Consequently, they used their influence to block some of the Commission’s more ambitious proposals.

The member state resistance forced E.C. officials to make compromises. The standard method which the Community used to alleviate member state concerns was to provide them with roughly equivalent options which could be adopted to comply with a directive. When these options were combined with the detailed provisions Community officials favoured, a highly complex directive often resulted. For example, the 62 articles of the Fourth Directive, which regulates company accounts, contains 41 options open to the member states in addition to 35 options left to companies.

The difficulties involved with drafting precise, detailed directives, together with the need for political compromise, substantially hindered the development and enactment of E.C. company law measures in the 1970s and early 1980s. Frustrated by the lack of progress, Commission officials adjusted their approach. In order to speed up negotiations, they became much more willing to give member states latitude in responding to directives. Concomitantly, they shifted the emphasis away from harmonising member state company laws to ensuring that member states shared equivalent standards in important company and securities law areas. Also, they gave priority to reforms which would promote cross-border commercial activity, arguing that such activity would foster

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46 Buxbaum & Hopt, supra, note 18 at 233-34.
47 Ibid. at 17. This pattern has been repeated in contexts other than company law (see McGee & Weatherill, supra, note 40 at 582).
48 Supra, note 23; and Buxbaum & Hopt, supra, note 18 at 234-35.
49 Buxbaum & Hopt, ibid. at 233-36; European Commission, supra, note 21 at 11; van Hulle, supra, note 45 at 14-15 & 26; and interview with F.J. Broichagen, European Commission, DG XV, April 1990.
50 White Paper, supra, note 16 at 34-37, Appendix, Part II, s. VI; M.G. Warren, “Global Harmonization of Securities Laws: The Achievements of the European Communities” (1990) 31 Harvard Int. L.J. 185 at 191-92 & 197-98; and interview with K. van Hulle, European Commission, DG XV, April 1990. The Community’s change from a harmonisation to an equivalence emphasis was not restricted to company and securities law. Instead, the shift was part of a general approach adopted to help create a single market by 1992. See McGee & Weatherill, supra, note 40 at 582.
the development of the Community and would make the E.C. more competitive on a global level.\(^{51}\)

The Community's new approach yielded immediate dividends. The shift in emphasis has re-energised E.C. company and securities law reform and has contributed to a flurry of legislative activity.\(^{52}\) This does not mean, however, that drafting and enacting directives has become a simple business.

One reason problems still remain is the continued existence of migration concerns. For example, such concerns have hampered negotiations on a number of measures which Community officials hope will foster cross-border activity. One of these is the Tenth Directive, which would require member states to liberalise existing restrictions on mergers between companies located in different member states.\(^{53}\) It gives rise to migration concerns because member states which mandate employee participation in management decisions suspect that their companies will use cross-border mergers to escape their regulations.\(^{54}\)

The Commission responded to these concerns by including a provision in the Tenth Directive which exempted mergers that would hinder employee participation rights.\(^{55}\) Thus, German company legislation, which mandates employee participation in management for many companies, could continue to impose restrictions on a merger between a German company and a non-German firm if the resulting company did not provide for employee participation. This attempt at compromise did not succeed, however, because European industry and a number of member states which do not have employee participation requirements felt too many cross-border mergers could be blocked.\(^{56}\)

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\(^{53}\) Supra, note 27.


\(^{55}\) Art. 1(3) of the Tenth Directive.

\(^{56}\) Kolvenbach, supra, note 29 at 742-43; Raaijmakers, supra, note 38 at 97; van Hulle, supra, note 45 at 22; and N. Bourne, "EEC Developments in UK Company Law" (1990) 11 Bus. L. Rev. 119 at 119.
Harmonising employee participation requirements throughout the E.C. would eliminate the Tenth Directive impasse. This, however, will be difficult to do. An important objective of the proposed Fifth Directive is to harmonise employee participation rights in public companies incorporated in the Community. The E.C. will probably not enact the Directive in the near future. This is because a number of member states, led by Great Britain, oppose mandatory employee participation and are prepared to use their votes in the Council to block approval of the Fifth Directive, at least in its present form.  

Two other cross-border co-operation measures which have been affected by migration concerns are the E.E.I.G. Regulation and the European Company Statute. With these measures, the E.C. wants to provide optional structures which member state firms can use to co-operate or organise on a supranational level. Community officials know that the E.E.I.G. and the European Company Statute will only be used if the Community makes them attractive to business. On the other hand, these officials have appreciated that member states which have mandatory employee participation will block enactment of these measures if they think these entities can be used to evade their regulations.

These conflicting considerations have led Community officials to make some tortured compromise proposals. Their strategy succeeded with the E.E.I.G. The E.C. gained German support for the E.E.I.G. Regulation by agreeing to limit the number of workers which E.E.I.G.s can employ to 500, the minimum threshold at which German companies must provide for employee representation on their boards.  

Making compromise proposals has not yielded successful results, however, with the European Company Statute. The latest draft of the Statute contains an array of employee participation options. Still, the prospects of the E.C. enacting the Statute in its present form are slight since the draft has not alleviated German concerns about migration or neutralised British opposition to employee participation.

57On British opposition, see Department of Trade and Industry, supra, note 29 at 2-3; Kolvenbach, ibid. at 729-31; and B. Montgomery, “The European Community’s Draft Fifth Directive: British Resistance and Community Procedures” (1989) 10 Comp. Lab. L.J. 429 at 436-37 & 446-51. Italy and Ireland also oppose employee participation on boards (Buxbaum & Hopt, supra, note 18 at 261; and interview with A. Ioakimides, European Commission, DG XV, April 1990). Germany also has reservations about the Fifth Directive (Kolvenbach, supra, at 731).


59The provisions are set out in the Involvement of Employees Proposal which is discussed infra, note 64 and accompanying text. On opposition to the Statute, see Winter, supra, note 13 at xxvi & 159; Carreau & Lee, supra, note 21 at 507-12; Kolvenbach, ibid. at 782-83; Department of Trade and Industry, supra, note 29 at 6 & 9; and “Threatened by Thatcher” The Economist (3 June 1989) 68. The problem has vexed the E.C. for many years. See, e.g., Sanders, supra, note 29 at 96-99, and P.M. Storm, “Statute of a Societas Europaea” (1968) 5 C.M.L.R. 265 at 269-70 & 282-84.
B. Board Structure

Employee participation is one of two issues concerning board structure which has generated considerable controversy in the E.C. The other is two-tier boards. Under a two-tier board system, a supervisory board fulfils many of the monitoring functions attributed to the shareholders and non-executive directors under Canadian company law. Management of the company is left to a management board, which is appointed by the supervisory board.60 This format is mandatory in Germany for companies with more than 500 employees. The system is optional for all companies in the Netherlands and for public companies in Denmark and France.61

When the Commission issued its first Fifth Directive proposal in the early 1970s, it recommended that all public companies incorporated in the member states should have two-tier boards. At the same time, it recommended that companies established under the European Company Statute have the same structure. Great Britain, which entered the Community in the mid-1970s, balked at the Commission's proposals. This was because in Britain, like Canada, all companies use a one-tier board, and the British government opposed any Community tampering with this system.

The Commission responded to Britain's concerns by altering its proposals to allow for a single-tier option.62 The significance of this concession is debatable. This is illustrated by the most recent drafts of the European Company Statute and Fifth Directive. Both measures require the one-tier board, referred to as the administrative board or administrative organ, to select an executive component from among its members and to delegate managerial power to that body. They then regulate the non-executive and executive components in much the same way as they regulate supervisory and management boards.63

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63Arts 68-80 of the European Company Statute and arts 5-13 & 21(k)-(t) of the Fifth Directive, (1988 draft). See Welch, supra, note 60 at 92-93, and Hopt, ibid. at 1345. The European Company
The treatment of employee representation illustrates how closely the one and two-tier systems resemble each other. The Fifth Directive and the European Company Statute contain the same four basic employee participation options. The manner in which the four options operate differs only slightly for one and two-tier board companies.

Under the first option, which is based on German law, employees in companies with two-tier boards select between one-third and one-half of the supervisory board. Employees in one-tier companies, on the other hand, select the same proportion of the administrative board. With the second option, which is based on Dutch law, employees, together with shareholders, have the right to veto nominees to the supervisory board in two-tier companies and nominees to the administrative board in one-tier firms.

Under the third option companies must establish a separate labour representation body. Both the Fifth Directive and the European Company Statute stipulate that management would have to give this body substantial information on a regular basis and would have to consult with it prior to specified decisions. This system operates the same regardless of whether a company has a one-tier or two-tier board.

The fourth option, which operates identically whether a company has a one or two-tier board, allows management and employees to agree on the method of employee participation. This apparently open-ended alternative is significantly constrained. The Fifth Directive provides that management and employees generally must agree on one of the first three employee representation options. The European Company Statute stipulates that the agreement must give employees at least the information and consultation rights provided for by the third option.

Statute refers to the one-tier board as the "administrative board" and the Fifth Directive uses the term "administrative organ."

Arts 4 & 21(d)-(i) of the Fifth Directive (1988 draft) and arts 4-6 of the Involvement of Employees Proposal. Member states can limit the options available in some circumstances: Fifth Directive, art. 4(2), and Involvement of Employees Proposal, art. 3(5).


Under art. 4 of the European Company Statute and the 1983 draft of the Fifth Directive, the supervisory board or the administrative organ nominates potential candidates. Under art. 4(c) of the 1988 version of the Fifth Directive, shareholders and employees can also nominate candidates.

More precisely, if no agreement is reached, a standard model, provided by the law of the member state where the company is registered, shall apply. This model is to be in conformity with the most advanced national practices and must ensure that employees have at least the information and consultation rights provided by the third option. See art. 6, paras 6 & 8 of the Involvement of Employees Proposal.
One important difference between the European Company Statute and the Fifth Directive is that the Fifth Directive's employee representation options do not apply to all companies it governs. For example, the Fifth Directive only requires member states to impose the employee representation options on public companies which have over 1,000 employees. Also, it allows member states to give employees the option of waiving their right to participate in corporate management. The European Company Statute contains no equivalent limitations on employee representation.

C. Shareholders

Canadian company law focuses almost entirely on shareholder/management issues, while workers' rights are left to different legislative schemes such as collective bargaining and employment standards laws. Because the E.C.'s company law programme gives an important role to workers, shareholder issues are less prominent than in Canada. Still, Community company law has significant implications for shareholders on a number of levels.

The proposed Fifth Directive is potentially the most important E.C. measure for shareholders in public companies. One reason is that, if it is enacted, its employee representation options would restrict shareholder influence over board appointments in the companies it applies to. Under the first of the four employee representation options, shareholders would be precluded from choosing more than two-thirds of the members of the administrative board under a one-tier system and could not select more than two-thirds of the supervisory board members in companies with a two-tier board. With the second option, Dutch experience suggests that in companies which adopt it, shareholders would have to negotiate with employees and existing board members about the appointment of new directors.

Shareholders would have greater appointment powers in companies adopting the third option, which again provides for a separate labour representation body. Under this system, shareholders would have the sole authority to

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68 Supra, note 27, arts 4(1), (2) & 21b(2).
69 Ibid., art. 4(2), 21b(2).
71 Supra, note 27, arts 4(b) & 21(d).
select the administrative board in a one-tier system and the supervisory board in a two-tier system.  

The Fifth Directive also contains provisions regulating shareholder litigation, general meetings, proxies, voting and the adoption of annual accounts by the shareholders. From a Canadian perspective these are the central components of corporate law. The political controversy generated by employee representation and board structure, however, has thus far blocked any progress on the other matters in the Fifth Directive.

Because of the impasse, the Commission is considering separating employee participation from the other management/shareholder issues in the Fifth Directive. Commission officials think this might speed up negotiations on the non-employee participation matters. Whether the issues involved can be effectively segregated, and whether the member states will accept such a strategy, remains to be seen.

D. Capital Structure, Disclosure and Accounts

While the lack of progress on the Fifth Directive has limited the impact of E.C. company law measures on shareholders, the E.C. has enacted a number of company law directives which have important shareholder ramifications. The matters involved are also important for creditors, so they merit independent consideration.

One such matter is capital structure. The assumptions underlying the Community regulations in this area differ from those in Canada. Canadian company laws reflect the view that solvency concerns are best addressed by negotiations between companies and creditors and by bankruptcy legislation and related measures. The E.C.'s company law directives, on the other hand, seek to provide affirmative protection for creditors by regulating internal corporate financial structures. For instance, while Canadian corporate legislation does not require a company to have a prescribed amount of share capital, the Second Directive, requires public companies to maintain a minimum share capital of 25,000 European Currency Units, or ECU's (approximately $35,000 Canadian as of May, 1991 exchange rates).

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73Fifth Directive, ibid., arts 4(1), 4d, 21(a)(1) & 21(e).
74Ibid., arts 14-21 & 22-50.
75Interview with A. Ioakimides, European Commission, DG XV, April 1990.
76See generally Hadden, Forbes & Simmonds, supra, note 7 at 131-32 & 141-47; Dine, supra, note 44; and J.S. Ziegel, "Is Incorporation (With Limited Liability) Too Easily Available?" (1990) 31 C. de D. 1075 at 1086-89.
77Art. 6 of the Second Directive. The European Currency Unit is a component of the European Monetary System and its value is calculated on the basis of the value of a basket of member state currencies.
The different approaches to creditor protection are also illustrated by the response to the potential financial risk created by a company acquiring its own shares. Canadian corporate legislation simply prohibits such transactions when they prevent the company from being able to meet its debt obligations. The Second Directive, on the other hand, requires member states which allow public companies to acquire their own shares to impose a number of detailed and restrictive limitations on the process.  

Another topic that E.C. directives regulate which is important for both shareholders and creditors is disclosure. The First Directive is key here. It instructs the member states to require all companies to file with a public registry prescribed information, including the corporate constitution, the amount of capital subscribed, a list of persons authorised to act on behalf of the company and the annual accounts. While the First Directive mandates the filing of accounts, it says nothing about the contents. This has been left to other directives. The Fourth Directive, which the E.C. enacted in 1978, is the most important of these. The Directive, which applies to all member state companies, regulates the use of valuation methods and establishes minimum standards for the presentation and content of annual accounts and annual reports. It also prescribes standards for the auditing and publication of these documents.

The Fourth Directive has helped to harmonise the presentation of annual reports and has helped to nurture a European approach to corporate accounting issues. Still, accounting standards are far from uniform in the Community. One reason is that three E.C. members have not implemented the Directive yet. Another is that there are many important company accounting issues the Fourth Directive does not deal with, partly because accounting practices have evolved rapidly since the E.C. enacted it.

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78 Supra, note 23, arts 19-22; and H. Sutherland, et. al. eds, Fraser's Handbook on Canadian Company Law, 7th ed. (Toronto: Carswell, 1985) at 76-93.


80 For a further discussion, see C.W. Nobes, “The Harmonisation of Company Law Relating to the Published Accounts of Companies” (1980) 5 Eur. L. Rev. 38. Also relevant are the Seventh Directive (see infra, note 93 and accompanying text), and Eighth Directive (which deals with auditor qualifications).


82 Italy, Portugal and Spain are the member states. The European Court of Justice has held that their failure to take action does not relieve individuals in the other nine member states from the obligation of complying with legislation implementing the Fourth Directive. See Ministere Public v. Blanguermon (1990), case C-38/89 (unreported), summarised in Common Market Reporter, supra, note 35 at para. 95,571.
A third reason for the lack of harmonisation of European accounting standards is that the implementing legislation in the remaining nine member states is not fully co-ordinated. This is because the member states have made extensive use of the large number of options which the Directive gives to them. They have done this because, to a far greater extent than might have been expected with such a technical subject, accounting practices are shaped and influenced by the member states’ distinct social and economic environments.

E. Small Business

The Fourth Directive applies to all companies, regardless of how many shareholders or employees a company has and regardless of how much revenue a company generates. If the Fourth Directive applied without qualification to all companies, smaller businesses would find the regulatory burden to be very high. Consequently, the Fourth Directive has always made some concessions for smaller companies. Presently, member states may relax a significant number of the Fourth Directive’s requirements for companies which do not exceed two of the following three thresholds: a balance sheet total of 1,550,000 ECUs (about $2.2 million Canadian), an annual net turnover of 3,200,000 ECUs ($4.5 million Canadian) and an annual average of 50 employees.

During the latter half of the 1980s, the Commission proposed a number of amendments which would increase the scope of the Fourth Directive exemptions. Most importantly, the Commission recommended that member states be required to make exemptions for small business rather than simply being authorised to do so. In a Directive approved in 1990, the Council declined to adopt the mandatory approach, but nevertheless did expand the exemptions which member states could make. The 1990 Directive is part of a general attempt by the Community to give small businesses a higher profile in E.C. affairs. The Twelfth Directive, which the Council approved in 1989, is also part of this trend. It requires the member states to reverse their present policy and allow single-member companies.

83Art. 1.
84Arts 11, 44 & 47(2), as am. Directive 84/569, O.J. 1984, L314/28. Also, member states are authorised to relax some of the Fourth Directive’s requirements for companies with higher balance sheet, turnover and employee totals. See art. 27 of Fourth Directive.
86See supra, note 52.
87In addition, the Commission has created a new Directorate for small and medium sized enterprises (Winter, supra, note 13 at 154), and the Council has approved a series of recommendations to member states which are intended to improve the business environment for small and medium-sized enterprises (O.J. 1990, L141/55).
88On the member states’ law in the area and on this directive see P. Colle, “The Influence of the European Convention on Mutual Recognition of Companies and Legal Persons, and of the Direc-
Despite these attempts to accommodate small businesses, E.C. company law initiatives historically have been aimed more at larger, public companies than their smaller counterparts. This has been because E.C. officials have felt that public companies have a more significant impact on member state affairs and because drafting and negotiating company law measures has been easier when smaller companies have been excluded. The upshot has been that most proposed and enacted company law directives apply only to public companies.

F. Corporate Groups and Multinational Enterprises

Community officials feel that corporate groups and multinational enterprises have an important impact on the E.C.'s economic and social fabric. Consequently, the E.C. has enacted three measures dealing with the internal governance of complex corporate undertakings and is considering a number of others. In contrast, Canadian treatment of such issues has been confined primarily to case law. One of the three corporate group measures the E.C. has enacted is the Seventh Directive. It requires member states to oblige parent companies to draw up and publish consolidated accounts of subsidiaries whenever either the parent or the subsidiary is a public company. This stands in contrast to Canadian corporate law.

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90Like the Fourth Directive, the First Directive (see art. 1) and the Seventh Directive (see art. 4) apply to all companies with some exemptions for smaller businesses. All other directives apply only to public companies. The discussion here conceals some classification complexities. The member states each generally have one corporate form intended for large companies with numerous shareholders and another intended for smaller companies. The former are most accurately described as public companies and the latter as private companies, and most company law directives apply only to public companies. The primary difficulty with this classification is that businesses often do not use the corporate form which seems to suit them best. E.g., in Germany many large businesses with numerous shareholders use the private company, or GmbH, form (see supra, note 42). The various classes of corporation in the member states are discussed in Brebner et al., supra, note 61.


92See Sargent, supra, note 7 at 163-79, and Hadden, Forbes & Simmonds, supra, note 7 at 625-28.

rate legislation, which imposes no such requirement. The Seventh Directive's underlying rationale is that group accounts must be analyzed to get a full and accurate impression of the overall financial status of a corporate group.

The Seventh Directive sets out the valuation principles and the format to be used for consolidated accounts. It also stipulates the types of linkages which require companies to prepare such accounts. For example, it mandates companies to do so if they own a majority of the voting shares of another company or have control of a majority of shares of another company by way of a shareholders' agreement. The Seventh Directive also requires companies to prepare consolidated accounts when one company has appointed the majority of the board members of another company by voting its shares, and when a company otherwise has the legal right to appoint the board members of another company. Moreover, the Seventh Directive gives member states the option to require consolidated accounts to be prepared when one company exercises a dominant influence over another.

The Eleventh Company Law Directive is the second measure the E.C. has enacted that is directly relevant to complex corporate undertakings. It deals with disclosure by company branches. The Directive's objective is to eliminate differences between disclosure requirements for company branches and subsidiary companies.

The Eleventh Directive only applies when a company establishes a branch outside its home jurisdiction. The Directive provides that a branch must disclose in its host member state most of the information about the company which the company is obliged to disclose in its own member state pursuant to the First, Fourth and Seventh Directives. At the same time the Eleventh Directive prevents the branch's member state from requiring any additional information about the branch.

The third measure the E.C. has enacted which is relevant to complex undertakings is the E.E.I.G. Regulation, which can be used by firms which want to establish co-operative cross-border arrangements. The Regulation's most

94Hadden, Forbes & Simmonds, supra, note 7 at 627. Canadian corporate legislation does contain some provisions regulating companies which prepare consolidated accounts: see, e.g., Canada Business Corporations Act, R.S.C. 1985, c. C-44, ss 157 & 160(5).
95Arts 1(a) & (d)(aa).
98Arts 1(1), 2-4.
99Arts 5-7. See generally Murphy, supra, note 51, and Israel, supra, note 58.
distinctive characteristic is that it provides an organisational framework which is not exclusively wedded to the legal system of any member state. Member state firms can create an E.E.I.G. by simply entering into a contract in accordance with the Regulation, though the grouping has to be registered in one of the member states.  

The contractual nature of E.E.I.G.s gives their members considerable freedom in organising grouping affairs, but the freedom is not absolute. E.E.I.G. members are deemed to be jointly and severally liable for the grouping's debts and must appoint natural persons to act as managers. E.E.I.G.s cannot invite investment from the public and, as mentioned, cannot have more than 500 employees. They can only engage in activities which are connected with their members' activities and their activities cannot dominate those of the members. Profits made by an E.E.I.G. cannot be retained by the grouping and instead must be apportioned among the members. The upshot is that E.E.I.G.s will generally have to be used for research and development ventures, co-operative training, marketing and testing programmes and joint bidding on projects.

E.C. officials hope to provide Members State firms with a number of other ways to organise on a Community-wide level. They give this priority because they feel that member state businesses must develop on a European basis to compete successfully with non-E.C. multinationals. Mergers between member state companies would be a logical way for cross-border reorganisation to occur, but mergers of this type are difficult to carry out. Member state company legislation generally requires unanimous shareholder consent for such transactions, which is impossible to obtain in most public companies. Also, member state tax legislation imposes significant financial obstacles. The Commission has recently sought to encourage cross-frontier mergers in two ways. One is by obtaining Council approval for a number of measures designed to reduce the tax...
obstacles.\textsuperscript{107} The other is by attempting to secure enactment of the \textit{Tenth Directive}. If enacted, it would preclude member states from requiring that mergers be approved by more than two-thirds of the shares voted.\textsuperscript{108} Hence, the barrier to mergers imposed by unanimous shareholder consent would be removed.

Otherwise, the \textit{Tenth Directive} would extend many of the \textit{Third Directive}'s provisions to cross border transactions.\textsuperscript{109} The \textit{Third Directive}, which the E.C. enacted in 1978, applies to mergers of companies from the same member state. It stipulates that prior to a merger the management of the companies involved must each prepare a report on the proposed transaction and must each appoint an independent expert to do the same. Each company must then make the reports available to the shareholders before they vote on the proposed merger.\textsuperscript{110}

As well as fostering mergers, Community officials would like to make the European Company available as a way for businesses to reorganise on a European level.\textsuperscript{111} This is reflected in the methods of incorporation set out in the most recent Commission proposal, which was made in 1989. They indicate that the \textit{European Company Statute} is much more concerned with fostering relationships between existing member state companies than it is with providing natural persons with an incorporation device. The three methods are a merger between E.C. public companies, the establishment of a joint holding corporation by such companies and the formation of a joint subsidiary by Community undertakings.\textsuperscript{112}

The 1989 draft regulates capital structure, share rights and restrictions, general meetings, accounts and corporate governance. The provisions are borrowed largely from existing and proposed company law directives.\textsuperscript{113} Consequently, as has been discussed, the one and two-tier board structures and the employee participation options are very similar to their counterparts in the \textit{Fifth Directive}.

\begin{footnotes}
\item[107] See Common Market Rep., \textit{supra}, note 35, paras. 95,594 & 95,678.
\item[109] On the transactions covered, see art. 3 of the \textit{Tenth Directive}.
\item[110] Arts 5-11.
\item[112] Art. 2. The proposal also stipulates that regardless of how a European Company is formed, it must have a minimum share capital of 100,000 E.C.U.s (about $140,000 Canadian) (\textit{supra}, art. 4(1)).
\item[113] Department of Trade and Industry, \textit{supra}, note 29 at 4-6, and interview with A. Ioakimides, European Commission, DG XV, April 1990.
\end{footnotes}
Employee participation concerns, as mentioned, have slowed progress on both the Tenth Directive and the European Company Statute. Two other proposed directives which are relevant to corporate groups have also encountered political problems. These are the Ninth Directive and the Vredeling Directive.

In most member states, as in Canada, company law treats subsidiaries as being largely autonomous from their parent. This gives parent companies a significant degree of flexibility, but also creates the possibility that a parent company, acting in its own interests, will act contrary to the interests of shareholders, creditors and employees of a subsidiary. The Ninth Directive would make important changes to these dynamics in Europe if the Community enacts it.

The Commission drafted the Ninth Directive in the early 1980s, but has yet to propose it formally to the Council. Its key concept is the control contract, which is known only to German law. Under the Ninth Directive’s control contract, a subsidiary company would consent to being controlled by the parent and the parent would become bound by two significant obligations. One is that the parent would have to buy out shareholders in the subsidiary who request this at the time the control contract is entered into. The other is that the parent would have to compensate a subsidiary’s shareholders, employees and creditors for losses they suffer as a result of the parent’s influence over the subsidiary.

The responsibilities and liabilities imposed by control contracts would make them unpopular with most member state parent companies. The Ninth Directive responds by creating a procedure which is designed to encourage parent companies to enter into control contracts. The Directive provides that when a control contract has not been entered into, those managing subsidiary companies have to prepare a detailed, audited annual report on the parent-subsidiary relationship. Any shareholder, creditor or employee of the subsidiary who feels, after reading the report, that the subsidiary’s interests have been prejudiced by the parent, can apply to a court in the parent’s jurisdiction. If the court finds that

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114Hadden, Forbes & Simmonds, supra, note 7 at 620-25.
116See Hadden, Forbes & Simmonds, supra, note 7 at 645, and Hofstetter, ibid. at 580-81.
117Indeed, control contracts are rarely used in Germany (Hadden, Forbes & Simmonds, ibid. at 581).
the parent’s board of directors has failed to act with due care and in the best interest of the group, the judge can impose joint and several liability for any losses on the parent company and the individual members of the parent’s board.

While the Ninth Directive regulates relations between members of a corporate group, the Vredeling Directive deals with relations between employees and management. The objective of the Vredeling Directive is to ensure that parent companies keep employees in subsidiary companies informed about group affairs. The most recent draft of the Directive, which the Commission submitted to the Council in 1983, imposes two basic disclosure obligations. First, it requires parent companies, referred to as dominant undertakings, to disclose annually to their subsidiaries enough information to give “a clear picture of the activities of the dominant undertaking and its subsidiaries taken as a whole” so this can then be communicated to representatives of the employees. Second, it requires parent companies contemplating decisions which are likely to have a substantial effect on the interests of the group’s workers to forward information to affected subsidiaries prior to the decision.

With decisions which would substantially affect employees’ interests, the 1983 draft mandates not only that employees be informed but also stipulates that they be consulted. These consultations are to take place with management of the subsidiary the employees work for. The objective of the process is an agreement between management and the employees’ representatives about the effect of the proposed decision on the employees.

The political battles which stalled the Ninth Directive and the Vredeling proposal were different from those involving the Fifth and Tenth Directives and the European Company Statute. This is because of the involvement of groups from outside the European Community. U.S. multinationals, which are heavily

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119The Commission first proposed the Vredeling Directive in 1980 (supra, note 34). Neither the 1980 or the 1983 version applies to all corporate groups. The 1980 version does not apply to subsidiaries with less than 100 employees (art. 4) and the 1983 version only applies to corporate groups with at least 1,000 employees in the E.C. (art. 2(1)).

120Art. 3(1). The information has to include the group’s economic and financial status, employment situation and future plans and prospects (art. 3(2)).

121Decisions giving rise to this obligation include the closure or transfer of major parts of an establishment, substantial modifications to the activities of a subsidiary and major organizational changes. See ibid., art. 4(2).

122Arts 4(1) & (3).
involved in the E.C. market, were distressed when the E.C. proposed the Ninth Directive and the Vredeling Directive. The multinationals were upset because these measures made only minor concessions to non-E.C. parent companies and thus would have imposed unfamiliar and unwanted obligations on U.S. business in Europe. U.S. business interests responded by heavily lobbying the E.C. institutions, arguing that investment in Europe would decline if these measures were enacted. U.S. congressmen also proposed retaliatory legislation.

These strategies succeeded. During the late 1980s, the Community essentially dropped the Ninth Directive and the Vredeling Directive from its agenda, partly because E.C. officials were concerned about allaying fears that the Community was evolving into a protectionist "Fortress Europe."

The E.C., however, may now be prepared to confront the issue of informing group employees again. Commission officials may soon submit a directive to the Council which would apply to companies if they operate in more than one member state, employ more than 1,000 people in the E.C. and employ at least 100 people in two or more member states. The intention of the proposed Directive is to provide information to employees rather than give them managerial influence. The Directive would require a company to inform its works council of major strategic decisions the company was planning. The works council, however, would have no consultative rights.

It is unclear whether, despite its more moderate approach, this new works council proposal is any more likely to be enacted than the Vredeling Directive.

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124 The Ninth Directive in fact is more disadvantageous for non-E.C. parent companies than it is for E.C. parents because it gives them less flexibility than E.C. parents in responding to buyout requests arising from the creation of control contracts (Carr & Kolkey, supra, note 115 at 65-66). The 1983 draft of the Vredeling Directive authorises non-E.C. parent companies to appoint an agent company in the E.C. to discharge its obligations. If no such agent is appointed, each E.C. subsidiary is responsible for disclosing the relevant information. See supra, note 34, art. 2(2).


126 Common Market Reporter, supra, note 35, paras 95 & 681.
European businesses have already objected to the new proposal and U.S. companies may do likewise since the measure apparently will apply to corporate groups which have headquarters outside the Community. On the other hand, many Community officials feel that it is very important for the E.C. to have social objectives so that workers can enjoy the benefits of integration. Consequently, the E.C. may press ahead despite the opposition.

G. Securities Regulation

The corporate securities market is far less developed in most member states than it is in North America. Only Great Britain has a stock exchange and diversified share ownership on a scale comparable with the U.S. and Canada. Other member states generally have small stock exchanges, populations which are sceptical about investing in securities, and few companies with widely traded shares. Moreover, takeover activity is significantly constrained by barriers imposed by company law, securities regulation and institutional factors. The institutional factors include substantial cross-ownership of shares between companies and a high level of share ownership by banks.

The securities market in Europe may be changing, however. The 1992 project has motivated business to reorganise on a European basis. As part of this process, mergers and takeovers have become more common. Also, the E.C. has been attempting to liberalise member state capital restrictions and if these efforts are successful, funds may be freed up for investment in corporate secu-

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128 "Don't Forget", supra note 35 and "E.C.", supra, note 35.
129 Pitts, supra, note 2 at 84-90; "Europe's Social Insecurity" The Economist (23 June 1990) 13; and B. Roberts, "The Social Dimension of European Labour Markets" in Dahrendorf, supra, note 40, 39.
132 This is illustrated by the Milan Stock Exchange ("Time for Change" The Economist (9 June 1990) 81).
rities. Finally, the E.C. has been quickly developing a Community-wide securities regulation framework.

Still, E.C. officials appear to be somewhat ambivalent about the operation of market forces in the securities area. Takeovers play a key role in the operation of British, U.S. and Canadian stock exchanges. Nevertheless, the Commission is unsympathetic towards them, arguing that they are an excessive and sometimes abusive method of restructuring.

The proposed Thirteenth Directive reflects the Commission's attitude. The Thirteenth Directive, if it is enacted, would make only a small dent in existing takeover barriers. Its primary effect would be to require member states to increase protection for the target's shareholders after a bid has been made. The Thirteenth Directive consequently might make it more difficult, if anything, to make a successful hostile bid.

Even though the Thirteenth Directive has not yet been enacted, the Community already has a number of securities measures in place. One example is the Insider Trading Directive, which the E.C. enacted in 1989 and which requires E.C. members to pass legislation prohibiting insider trading by June 1992.

At present, a number of member states do not regulate insider trading at all and most others do not do so with any rigour. Consequently, the Insider Trading Directive could potentially reverse current Community policy. Certainly, the Directive is very broad in scope. It defines insider information liberally,

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135 Supra, note 33, art. 8, as amended by O.J. 1990, C240/7; Basaldua, supra, note 131 at 499, and interview with A. Ioakimides, European Commission, DG XV, April 1990.

136 Arts 4, 10, 12 & 14. See Keim, supra, note 133 at 571-75. Articles 4 and 10 have been changed slightly by O.J. 1990, C240/7.

137 See Basaldua, supra, note 131 at 495-500, and MacLachlan & Mackesy, supra, note 131 at 398-99. The Major Shareholdings Directive, Directive 88/627, O.J. 1988, L348/62, will probably have a similar effect. It requires shareholders in companies listed on stock exchanges to disclose the extent of their voting rights upon the acquisition or disposition of shares at 10%, 20%, 33 1/3%, 50% and 66 2/3% of the company's outstanding voting rights. The disclosures should give boards of target companies more time to take defensive measures against hostile bidders.

138 Supra, note 32.

employs a broad definition of insider and prohibits insiders from engaging in a wide range of activities.\textsuperscript{140}

In practice, however, the Directive may not bring dramatic changes. This is because of its treatment of enforcement. The Directive only requires member states to appoint an authority with sufficient powers to regulate insider trading and to establish sanctions which are sufficient to promote compliance. These requirements are open ended enough to allow member states which saw little reason to regulate insider trading in the past to follow much the same pattern in the future.\textsuperscript{141}

The E.C. has also enacted a number of measures which are intended to provide investors with information about companies which make public offers of their securities. Taken together, the Admissions Directive, the Listing Particulars Directive, the Continuous Disclosure Directive and the Public Offer Prospectus Directive require member states to pass legislation which imposes disclosure and publication requirements on companies listed on Members State stock exchanges and impose similar, though less rigorous, obligations on companies which are not listed but which offer their securities for sale to the public.\textsuperscript{42}

The most notable characteristic of the disclosure directives is that in the late 1980s they were amended to introduce the concept of mutual recognition.\textsuperscript{143} The basic thrust of the mutual recognition principle is that an undertaking, product or service which has fulfilled one member state’s requirements should be accepted by all E.C. members when the member states have essentially equivalent standards.\textsuperscript{144} As applied to securities disclosure, mutual recognition means that when a member state’s regulatory authority approves a company’s disclosure documents, this approval must be accepted by the relevant authorities throughout the Community. Consequently, if a British company has complied with Great Britain’s legislative framework and wants to make a public offer in Germany, Germany’s disclosure requirements will not apply, even if they are stricter than Britain’s.

The mutual recognition principle potentially runs contrary to Europe’s traditional hostility to the possibility of migration from strict company law rules.


\textsuperscript{141}Arts 8 & 13; Buxbaum & Hopt, \textit{supra}, note 18 at 246-50; Warren, \textit{supra}, note 50 at 221; McGuinness, \textit{supra}, note 139 at 448-49, 451-52; and Stutz, \textit{ibid.} at 169-72.


\textsuperscript{143}The relevant changes were made by the Mutual Recognition Directive.

\textsuperscript{144}\textit{White Paper} at 6, 18-22, and Curzon-Price, \textit{supra}, note 40 at 29-30. Again, this was part of a general trend — \textit{supra}, note 50.
The Community-wide effect of approval by one member state will give companies making a public offering choice about the regulatory scheme under which they seek approval. This may cause E.C. members to adjust their legal standards and administrative rules to attract securities offerings. Some think this will lead to an irresponsible erosion of regulatory standards. The possibility exists, however, that the relevant regulatory schemes may become more responsive to the needs of E.C. companies and the investing public.\textsuperscript{145}

Regardless of whether any adjustments which take place are beneficial or not, the overall process will be constrained in important ways. The minimum standards established by the various securities disclosure directives will create a regulatory floor. Also, the directives themselves impose some constraints on forum shopping.\textsuperscript{146} Furthermore, many types of public securities offerings are not covered by the directives so they will not be affected by the mutual recognition principle.\textsuperscript{147} Finally, many companies will not find it cost-effective to apply outside their home country even though the legal rules may be somewhat more favourable elsewhere. Consequently, the mutual recognition principle should not create a regulatory free-for-all in the securities disclosure context.

IV. Canadians and European Community Company and Securities Law

While most E.C. company and securities law measures have aspects which may interest Canadian businesses, Canadian investors and Canadian law reformers, some issues merit detailed consideration here. These will now be examined from the perspective of the three groups.

A. The Business Community

Canadian businesses which pursue the E.C.'s commercial opportunities by establishing a permanent base in Europe will have to consider E.C. company and securities law. The two primary ways of establishing such a base are by forming a branch or a subsidiary company.\textsuperscript{148} Using a subsidiary has a number


\textsuperscript{147} Art. 2, discussed by Warren, \textit{ibid.} at 37-46.

\textsuperscript{148} On the ways non-E.C. companies can approach the E.C. market and the advantages involved with having a base there, see Pitts, \textit{supra}, note 2 at 157-58, 168-90, 212-14 & 218-29; and Winter, \textit{supra}, note 13 at 80 & 294-97.
of legal advantages. Most important, courts and governments will generally treat a subsidiary company as a distinct legal entity which is based in one of the member states. They will not do this with branches. This makes a significant difference, since member state companies are entitled to rely upon most of the freedoms guaranteed by the Treaty of Rome and the ownership structure of a company does not affect these rights. Consequently, a Canadian subsidiary, unlike a branch, generally should be able to fully exploit the benefits of the E.C.’s single market.\(^\text{149}\)

The E.E.I.G. Regulation and the European Company Statute illustrate why using a subsidiary is advantageous. Both place restrictions on their use by non-E.C. undertakings. Undertakings based outside the E.C. cannot be an E.E.I.G. partner and, under the most recent draft of the Statute, cannot be involved in the formation of a European Company.\(^\text{150}\) These restrictions would prevent a Canadian branch from using either business form but they would not be a problem for the European subsidiary of a Canadian company. This is because it would qualify as an E.C. undertaking, despite being owned by a non-E.C. firm.\(^\text{151}\)

If a Canadian company follows the branch route, the only E.C. company and securities law provision which should be directly relevant is the Eleventh Directive. Again, it regulates disclosure by branches in the member states. Of most significance for Canadian companies, it requires non-E.C. company branches to file prescribed information about the company.

A Canadian company which acquires or incorporates a subsidiary in the Community will be subject to E.C. company and securities law via the legislation of the subsidiary’s member state. Generally speaking, however, Canadian parent companies should not be directly affected by E.C. measures. This is because few of these measures require member states to impose obligations directly on non-E.C. parent companies.\(^\text{152}\) Even the Seventh Directive, with its focus on corporate groups, does not attempt to regulate non-E.C. companies. The only potential exceptions have not yet been enacted, these being the Ninth Directive and the directives dealing with disclosure to employees in corporate

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\(^\text{149}\) Arts 52, 58 & 59. Not all non-E.C. subsidiaries are assured of equal treatment with companies which are owned by E.C. interests. At the very least, non-E.C. subsidiaries will have to have a real and continuous link with the economy of one of the E.C. members. See generally Winter, \textit{ibid.} at 79-85; Ferry, \textit{supra}, note 126 at 223; Lee, \textit{supra}, note 126 at 18-19; and J.F. Dinnage, “Comments on the ‘Europe 1992’ Symposium” (1989) 3 Temple Int’l & Comp. L.J. 179 at 181-82.


\(^\text{152}\) Winter, \textit{supra}, note 13 at 151.
groups. If these measures are enacted, they likely would apply to non-E.C. parent companies which have European subsidiaries.153

A Canadian company that decides to use a subsidiary as its European foundation will have to choose which member state to incorporate in. The choice is made somewhat more difficult because a Canadian parent generally will not be able to incorporate its subsidiary in one member state and base its operations in another. This is because the real seat rule, which operates in most member states, prevents companies which have their business based in one member state from being incorporated in another.

The real seat rule likely imposes costs on non-E.C. companies.154 In deciding where to establish operations most companies would consider commercial and financial considerations to be more important than company law factors.155 Consequently, if the member state which has the most favourable commercial environment happens to have an unattractive company law regime, a Canadian parent will still likely decide to base its operations there. Nevertheless, the inconveniences imposed by that member state's company law will impose costs on the subsidiary and thus on the parent.156

Canadian companies might assume that because of the E.C.'s harmonisation programme, the differences between member state company laws will be minor and the costs imposed by disadvantageous legal rules should be slight. There is a problem, however, with this line of reasoning, which is that important differences continue to exist between member state company laws.157

153See supra, note 124, and E.C., supra, note 35.
154The rule strongly encourages non-E.C. parents to incorporate in the member state where they want to base their operations rather than in the member state with the most suitable company law.
155Pitts discusses other factors which would be relevant supra, note 2 at 229-33.
156E.g., a Canadian company might decide that commercially Germany would be the best place to establish a subsidiary. Germany, however, imposes worker participation requirements on its companies. A Canadian company likely would be unenthusiastic about the prospects of meeting this requirement, given that employee participation in management rarely occurs in Canada. See Pitts, ibid. at 241; Axworthy, supra, note 7 at 393-97 & 423-27; Hadden, Forbes & Simmonds, supra, note 7 at 291-93; and Carr & Kolkey, supra, note 115 at 63-64. Employee participation arguably could be beneficial for business, however. Its impact on the profitability of corporations has been debated extensively. See, e.g., Hopt, supra, note 62 at 1353-59; Daübler, supra, note 89 at 473-81; M.C. Jensen & W.H. Meckling, "Rights and Production Functions: An Application to Labor-Managed Firms and Codetermination" (1979) 52 J. Bus. 469 at 472-75 & 503-504; S.M. Weiss & R.L. Yaffe, "Industrial Democracy: A Study of the Bullock Report and its Applicability to Canada" (1979) 9 Man. L.J. 445 at 475-77; L.L. Dallas, "Two Models of Corporate Governance: Beyond Berle and Means" (1988) 22 J. of L. Ref. 19 at 75-80; and O.E. Williamson, The Economic Institutions of Capitalism: Firms, Markets, Relational Contracting (New York: Free Press, 1985) at 268-72 & 302-04.
157Also, there are a number of areas which are closely related to company law where no harmonisation has taken place and probably will not in the near future. These include winding-up and insolvency. See Encyclopedia, supra, note 11, vol. B at para. B10-487.
There are a number of reasons for why differences between company law regimes persist. One is that many topics have not been dealt with by enacted directives. For instance, the disagreements about employee participation and two-tier boards have not only prevented harmonisation in these areas, but have blocked passage of the Fifth Directive, which deals with a number of other key company law areas. Another reason is that some member states are slow to implement enacted directives. At present, only two of the seven company law directives which the member states are currently obliged to comply with have been implemented in all twelve member states.  

Furthermore, member state implementation does not always result in closely equivalent laws. The Fourth Directive experience, discussed above, illustrates this, but the problem is not an isolated one or one which will be eliminated easily. For example, enactment of the Fifth Directive might well do little to harmonise regulation of employee participation in management. Given that social and economic differences have helped to prevent harmonisation in the accounting area, the prospects for harmonisation in the politically charged area of employee/management relations seem to be rather bleak.

The European Company Statute theoretically could reduce some of the costs which the real seat rule imposes on Canadian parent companies. This is because it could provide a Canadian parent with a statutory regime for a subsidiary which was preferable to that in the member state where the parent company wanted to establish operations. Canadian parent companies should not be too optimistic, however, about the prospects of such a lower-cost alternative.

One reason, as has been discussed, is that employee participation considerations distinctly reduce the prospects of the Statute being enacted in the near future. Another is that Canadian businesses will have to endure some costs to form such a company. Again, under the most recent proposal, European companies can generally only be formed by the joint action of two or more E.C. firms. A Canadian parent which wanted to use the European Company form for its subsidiary would have to take some additional legal steps, such as forming subsidiaries in two member states and having them incorporate as a European Company.

A third reason the European Company Statute may not be attractive for Canadian businesses is that European companies will be governed to a significant extent by the laws of the member state where they are based. The 1989

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158 European Commission, "Implementation of the Company Law Directives in the Member states" (1990) [unpublished].
159 Buxbaum & Hopt, supra, note 18 at 233-43 & 263-66.
draft of the Statute requires a European Company to register in the member state where it has its central administration. Consequently, a Canadian parent would have to register the subsidiary in the member state where it was planning to establish operations. This is significant because the Statute leaves a number of important company law issues to be governed by the member state where registration has taken place. The result is that there may be few cost differences between the member state company law and the European Company Statute.

B. Investors

As mentioned in the introduction to this article, Canadian investors are becoming more interested in the E.C. market and are consequently acquiring increasing numbers of shares in European companies. If, however, investors are assuming the Community’s company law and securities regulation initiatives will enhance the value of shares in E.C. firms, they could be mistaken.

Arguably the centralising impulse inherent in E.C. company and securities law measures is contrary to shareholders’ interests. There is a strong trend of opinion in the U.S. that shareholders’ interests are best served when companies can select between legislative regimes to provide a package which will be attractive to shareholders. The real seat rule already severely restricts the ability of E.C. companies to make such choices. To the extent that E.C. company law directives successfully develop equivalent legal rules through the Community, companies will face even more serious constraints on their options.

Many would dispute that the development of uniform or equivalent rules across jurisdictions is contrary to shareholders’ interests. Still, even accepting

161 Supra, note 29, art. 5.
162 The European Company Statute expressly stipulates that regulation of corporate groups, mergers, insolvency and sanctions for breach of the Statute are to be governed by member state law. See arts 114, 129, 132 & 134. Also, there are important matters which the European Company Statute makes no reference to and which consequently would be governed by the law of the member state (see Department of Trade and Industry, supra, note 29 at 3 & 7-8). Finally, the courts of the chosen member state would interpret all disputes concerning the company’s internal affairs, and would probably do so in accordance with the prevailing principles of their legal system. The Statute provides, however, that matters covered by it but which are not expressly mentioned are to be interpreted in accordance with the general principles upon which the Statute is based (art. 7(1)).
163 Two commentators who have asserted that the same arguments are valid in the E.C. are L.S. Scally, “British and European Company Law” in Dahrendorf, supra, note 40, 89 at 97-101, and H.N. Butler, “Nineteenth-Century Jurisdictional Competition in the Granting of Corporate Privileges” (1985) 14 J. Legal St. 129 at 166 n. 150.
that harmonisation of Community company and securities law is generally beneficial to shareholders, particular E.C. measures may adversely affect them. Some would argue, for example, that if the Community’s attempt to discourage insider trading succeeds, this will decrease share values. The Fifth Directive likely would have the same effect if it is enacted. In most member states, it would shift power away from the shareholders to the employees. The evidence from Germany suggests that shareholders would be made worse off by such a shift.

This does not mean that investor enthusiasm about the E.C. is misplaced. The Community, by attempting to create a single market in the E.C. by the end of 1992, is altering the face of Europe. Admittedly, the E.C.’s single market project still faces political and technical obstacles. Nevertheless, the Community has made significant progress in meeting its 1992 timetable. Probably even more important, E.C. businesses, as mentioned, are now “thinking European” and are planning and reorganising on an E.C. level. In addition, the 1992 project has had a significant psychological impact on member state companies. Consequently, the companies should be more receptive to the European focus of the Community’s company and securities law initiatives.

No doubt some companies will lose out in the development of the single market. Still, most expect that the overall economic impact will be strongly beneficial for European business. If this is accurate, the effect should outweigh any potential negative fallout from E.C. company and securities law. Hence, Canadian investors who properly diversify their European investment portfolio likely will benefit by increasing their holdings of European securities.

C. Law Reformers

Canadians interested in corporate law reform may be able to benefit from increasing their knowledge of the E.C. Canadian corporate law has been drawn

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166Hopt, supra, note 62 at 1356.


169Ibid. at 71-73, 76 & 82; “Post-‘92,” supra, note 3; United States International Trade Commission, supra, note 54 at 2-6 – 2-12; and “Cashing In on European Integration” The New York Times (30 April 1989) s. 3, 10. See, however, M. Porter, “Europe’s Companies After 1992: Don’t Collaborate, Compete” The Economist (9 June 1990) 17.
substantially from U.S. and British sources.\textsuperscript{170} Similarly, Canadians have most often borrowed theoretical perspectives from these jurisdictions. Law and economics analysis, which emerged in the U.S., is the latest example.\textsuperscript{171}

The E.C. provides a potential alternative source of corporate law ideas. There are important similarities between the Community and Canada which make comparisons relevant and potentially revealing. As mentioned, in the E.C. cross-ownership of shares is common and only a few companies have widely traded shares. Though the situation is not as extreme as in the E.C., these characteristics are more prevalent in Canada than they are in the U.S.\textsuperscript{172} Also, in both the E.C. and Canada there is divided legislative responsibility for company law and securities law matters. Thus, these matters are regulated by provincial or member state authorities on the one hand or the federal or Community authorities on the other.

Several Canadian observers have in fact already drawn on E.C. company law to enhance and illuminate their work. For example, a number of Canadians have written about the E.C. approach to employee participation in management, board structure and corporate groups.\textsuperscript{173} There are other matters, however, which merit consideration.

For example, Canadians who favour increased uniformity in provincial legislation should find the mandatory, binding directive system an attractive alternative to the Canadian situation, where there are no mechanisms available to force the provinces to adopt uniform legislation.\textsuperscript{174} On the other hand, the history of corporate law reform in the E.C. and Canada suggests that institutional structures are not always key to developing uniform legislation. While the E.C.'s attempts to harmonise company law have run into significant obstacles, the absence of an institutional framework has not prevented the emergence of substantially uniform Canadian corporate legislation in recent years.\textsuperscript{175}

Canadian observers who support a decentralised approach to legal regulation may also find the E.C. company and securities law to be of interest.\textsuperscript{176} The

\textsuperscript{170}Hadden, Forbes & Simmonds, supra, note 7 at 24-33.


\textsuperscript{172}R.J. Daniels & J.G. MacIntosh, “Toward a Distinctive Canadian Corporate Law Regime” (1990) [unpublished].

\textsuperscript{173}Supra, note 7.

\textsuperscript{174}Cuming, supra, note 164 at 11. On the problems with harmonisation mechanisms in Canada, see supra at 28-47 & 52-55; Ziegel, supra, note 164 at 10-28 & 44-49; and Hurlburt, supra, note 164 at 401-15.

\textsuperscript{175}Cuming, ibid. at 24-25; Ziegel, ibid. at 34; and Hurlburt, ibid. at 399.

mutual recognition principle seems particularly attractive. This is illustrated by provincial regulation of disclosure by companies issuing securities to the public.

Individual provincial vetting of prospectuses and continuous disclosure documents imposes compliance costs on corporate issuers. Most often these costs are needless, since the provincial regulator with whom the documents are initially filed should detect any serious errors. Provincial securities regulators have responded to the problem by trying to reduce the filing requirements for issuers which have had their documentation accepted where it was initially filed. This is useful, but the underlying assumption still is that each province's regulatory requirements must be met. Consequently, a shift in emphasis might be appropriate. The E.C.'s principle of mutual recognition could provide the inspiration for such a shift. If this principle were applied in Canada, documents accepted by one provincial securities regulator would be acceptable in every other province. If this were felt to be too liberal, provincial legislatures and securities regulators could create specified exceptions to protect against potential irresponsible abandonment of regulatory standards. The result would still likely be reduced costs for corporate issuers and a smaller regulatory bureaucracy in most provinces.

Conclusion

The European Community is one of the world's most important economic and political institutions, and recent events suggest its importance will continue to grow. Because of these factors, Canadians have a strong incentive to become and remain informed about Community topics. For example, Canadian businesses, investors and law reformers have good reasons to examine E.C. company and securities law.

Canadians who decide to analyze Community developments must ensure that they have some understanding of the context in which the developments are taking place. For example, the most striking E.C. company law measures probably are the Fifth Directive, the Ninth Directive, the European Company Statute and the directives dealing with disclosure to employees in corporate groups. This is because these measures are socially and politically controversial as well as legally significant. Consequently, it should not be surprising that Canadians

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who have examined E.C. company and securities law have focused on issues dealt with in these measures, including, as mentioned, employee representation in management, board structure and corporate groups.

Analyzing these topics in isolation, however, gives a misleading impression about E.C. company and securities law. Only by considering the E.C.'s institutional mechanisms and political dynamics can one appreciate that the Fifth Directive, the Ninth Directive, the European Company Statute and the directives dealing with disclosure to employees in corporate groups are surrounded by political controversy and may not be enacted in the near future. Similarly, only by examining other E.C. company and securities law measures can one appreciate that the Community has already enacted a significant number of provisions which are potentially important to a Canadian audience.

This lesson is not an isolated one. Each Community topic which might be of interest to Canadians, whether it is E.C. trade policy, competition law, financial services regulation or another matter, will have aspects which cannot be properly understood without some appreciation of the institutional and political context. Canadians who are interested in the E.C., and those writing about the Community for a Canadian audience, should remain aware of such considerations. If this admonition is kept in mind, interested Canadians should be able to develop a well-balanced and thorough understanding of a very important legal, economic and social institution.