LEGAL ASPECTS OF DOING BUSINESS IN WESTERN EUROPE

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INTERNATIONAL BUSINESS SERIES

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JACK J. COE JR.

Introduction

For business and its legal counsel the Western European marketplace represents challenge and opportunity. In even the most basic of transactions, legal facets are numerous. The complexity and interdependence of legal, political, monetary and economic systems which characterizes the modern business arena generally are epitomised in Europe. The imposition of supranational 'European' law upon the national legal systems of the ten Member States of the European Community (EC), themselves a combination of Common Law, Civil Law and hybrid systems, is but one aspect of legal superstructure. Coexisting with, and to some extent complementing, such on-going alignment are the strands of uniformity lent to transnational commercial law through the work of such bodies as The International Institute for the Unification of Private Law (Unidroit) and The United Nations Commission on International Trade Law (Uncitral).[1]

Despite increasing uniformity, however, in order to prepare advice reflective of the whole of his client's transnational activities, legal counsel involved in Europe must don the garb of the comparativist. Often, in close liaison with local counsel, general business counsel is called upon to synthesise diverse and sometimes conflicting national and supranational policies and supporting legal rules and to do so with sufficient foresight to assist in initial investment planning. Cultural, geographic and linguistic differences, of course, add to the challenge as do occasional shifts in governments' political orientation. The spectre of trade protectionism, too, enters the calculus.

At the same time, Europe's expanding economic and political unity continues to afford investment opportunities.[2] European governments continue to compete for foreign investment, particularly labor-intensive varieties, and trade channels such as those facilitated by the more than eighty-three trade links existing between the EC and third countries continue to be refined.

In preface to the more detailed chapters which follow, the following pages seek to identify some of the structural components and areas of concern which characterise the trade and legal environment in Western Europe. The European Community, its objectives and supporting legal régimes will receive special attention by way of the selective overview which follows. Final pages then will highlight some broad areas of concern relevant in developing an approach to Europe.[3]

The European Community

It is difficult to generalize about the importance of the European Community.[4] Its policies, legal rules and market potentialities will vary with the nature of business activity envisioned. Nonetheless, it is perhaps safe to suggest that the days have all but disappeared during which Community policies and supporting legal rules can comfortably be disregarded by international business.

The imposition of Community law upon national law is a process which increasingly will affect business conduct throughout Europe. Through the harmonisation of national laws, the thinking of those who interpret and implement the Treaty of Rome dictates the future content of national regulations in areas as fundamental as company law, taxation, and intellectual property. Thus, the monitoring of developments emanating from Brussels has become a prerequisite to planning compliant modes of action and to contributing to the process constantly shaping the legal and economic environment. Part of the challenge facing business management and its legal counsel therefore is to strike an appropriate balance between complete ignorance of, and undue preoccupation with, the prolific activities of the Community's decision-making bodies.

A corollary of continuing economic and legal integration within the Community is the enhanced attractiveness of Europe as a potential market. As non-tariff barriers subside and the free circulation of goods and services is ensured, the feasibility of reaching a potential market of 260-million consumers consequently will be increased, allowing firms more readily to formulate market strategies embracing the entire Community and beyond. With the continued increase in EC membership will come added opportunities. Spain, for example, upon joining the EC would become, according to one expert 'the best potential growth market of the Community during the next ten years'.[5]

The European Economic Community (EEC): Concept and Scope

The Treaty of Rome contemplates more than the creation of a free-trade zone and indeed more than a customs union. Its concept transcends purely economic objectives. Envisioned is a politically and economically united zone within which goods, capital, ideas, and people will be able to move freely. The reciprocal effect aspired to is an alleviation of the long-standing confrontation of national economic interests which historically has resulted in disruptive protectionism.[6] The intercourse envisioned is embodied in the Treaty's 'four freedoms': free movement of goods,[7] persons,[8] services[9] and capital.[10] By design the process will involve:

> 'a gradual but substantial integration of national economies under the aegis of a supra-national organization which is destined to take over the traditional functions of states to regulate the economy, to adopt a common monetary system, a central banking organization, a uniform tax system and a single external trading policy'.[11]

The vision contemplates in part that through economic integration an otherwise unattainable political integration will be facilitated.

Within Europe, many of the Community's policies affect the pursuits of international business.[12] Most fundamental are those addressed to internal and external trade and in particular those associated with the Customs Union and Common Commercial Policy. The former has been largely achieved and consists in the following components:[13] (1) the abolition of customs duties, (2) common customs legislation, (3) the pooling of customs revenue, and (4) a Common Customs Tariff (CCT) applicable at the external frontiers of the Union. The latter ingredient is a key factor in enabling goods emanating from the non-Member States to circulate freely within the Community once relevant duties have been paid and requisite formalities observed. More specifically, the CCT, a system of common classification and tariff, means in theory that exports into the EC need clear customs only once before reaching a vast market of consumers. By law, no Member State's government may erect import restrictions arbitrarily, but rather must take protective action only in compliance with Community procedures. Such extraordinary measures ordinarily assume the existence of severe economic difficulties within the relevant sector.[14]

Tariff barriers are but one obstacle to the free cross-boundary movement of goods in Europe. In the implementation of the CCT, problems of documentation, valuation, and categorisation remain formidable. In addition, variations in rates of value added tax (VAT), or in health and safety standards contribute to reduced interchange within the Community. Thus, much of the work of the relevant Community institutions has involved the harmonisation of customs laws and other non-tariff barriers.[15]

The Common Commercial Policy (CCP) is the second support on which the Community trade policy relies.[16] It complements the Common External Tariff by ensuring, in theory, that the Community speaks uniformly and with a single voice when dealing with external trade partners. Thus, third countries seeking to negotiate bilateral agreements with a Member State must deal with a Community institution, specifically the Commission of the European Communities. Such negotiations involve, *inter alia,* CCT amendments in light of variations in trade, commercial, and political relations between the Community and the non-member country involved.[17]

Principal Community Institutions and the Decision-making Process

Decision-making in the Community is a function of the interplay between the Commission and the Council of Ministers.[18] Composed of Commissioners appointed jointly by the Member States, the Commission's main functions are to study problems and propose solutions in the form of legislation, and to execute the duties of the three communities through regulations, directives, and decisions.[19] The Commission also serves as a mediator among Member Governments. The Council of Ministers comprises one Minister from each Member State, though that Minister changes according to the subject being discussed. When transport legislation is being drafted, for example, the Trans-

port Minister from each Member State serves. The Council's importance functionally is that absent its acceptance, legislation proposed by the Commission will not become law. Generally, such approval requires unanimous consent. Predictably, the resulting veto power leads to much political bargaining among Ministers. Much proposed legislation is never accepted by the Council.[20]

Related to the Council is the Committee of Permanent Representatives (COREPER). A collective of Ambassadors of the Member States, it is charged to 'prepare the work of the Council and to carry out the tasks assigned to [them] by the Council'.[21] In addition to providing a forum where Member States articulate national policies and attitudes, the COREPER does much of the routine work of the Council, the latter convening only at intervals.[22]

A third institution which directly affects the law of the Community is the European Court of Justice (ECJ).[23] It comprises ten judges, neutral but representing by origin the ten Member States and four Advocates General[24] selected from the four largest Member States.[25] The Court exists to render preliminary rulings on points of law submitted by national courts, to advise the institutions, and to adjudicate in contentious proceedings, which either involve actions against Member States to enforce their treaty obligations or against Community institutions. The Community's 'federal' scheme leaves to the Member States' national courts the 'application' of Community law. The ECJ as 'interpreter' of Community law, however, has a significant role in shaping Community economic law,[26] and the body of judicial opinion with which it is credited is an authoritative secondary source of law with which European business must become and remain familiar.

The European Parliament[27] constitutes a fourth principal institution of the communities. Also referred to as the 'Assembly', its function as defined by the Treaties is to exercise supervisory powers. It is composed of representatives from the Member States elected by each Member State. The parliament has no legislative powers and limited budgetary power and according to the treaty is merely a deliberative and consultative body. Its workings are characterized by specialist standing committees, debates, reports, working papers and its methodology includes an effective procedure of questioning the Council of Ministers and the Commission.

Community Law – Its Mode and Content

Having a federal structure, the Community displays a division of functions between supranational and national systems.

> 'Within the specific domain of the Community, i.e. for everything which relates to the pursuit of the common objectives within the Common Market the institutions [of the community] are provided with exclusive authority. . . . Outside the domain of the Community, the governments of the Member States retain their responsibilities in all sectors of economic policy. . . . They remain master of their social policy; the same undoubtedly holds true for large segments of their fiscal policy . . .'[28]

Where the two conflict, however, Community law supersedes a Member State's domestic law.[29]

Community law is based on three pieces of primary legislation or treaties, and various forms of secondary legislation. Those latter instruments include regulations, directives, and decisions and are distinguished by the method and extent to which they become part of Members' domestic law. Thus regulations, which are binding on Member States in their entirety and which are of direct effect, are distinguished from directives which are legally binding on Member States with respect to the aim to be achieved but which depend on implementation through national legislation within the particular Member States.[30] Most legislation affecting European business is precipitated by directives[31] so that some uniformity is lost to national idiosyncrasies. Directives often remain in draft form for months and even years. Industry, therefore, has sufficient opportunity to voice its concerns, which it traditionally has done both at the Commission and Council stages of consideration.[32] In addition, proposed and draft directives may be monitored by interested businesses through such agencies as the United Kingdom's Department of Trade.

Decisions are formulations directed to a specific problem and often directed to a specific individual or company. Like regulations and directives, decisions are binding instruments which should be contrasted to recommendations and opinions. The latter two, while important as indicators of present and future policy, are not legally binding.[33] The concept and content of European law is a formulation which reflects common features of the Member States' legal régimes, yet which is not based solely on one particular national system. Functionally, European law is servile to the broader objectives of economic and political integration within the Community. Legal integration as a means to an end may be deemed an evolutive process characterised by ongoing approximation, harmonisation and co-ordination of national laws.[34] The resulting legislation may be a uniform body of law which supersedes corresponding domestic rules, or which creates entirely new uniform rules. Alternatively, legislation may seek to imbue existing national legislation with a greater degree of compatibility through the superimposition of common criteria and policy objectives.[35] The ultimate goal is not the creation of a vast body of unique European law but rather, within an essentially federal structure, an alignment of national legislation 'to the extent required by the proper functioning of the common market'.[36]

> 'In practice harmonization has served mainly to eliminate technical barriers to trade and to impose Community standards of goods and marketing. Such harmonization measures are usually drafted in considerable detail leaving little discretion to Member States. Taken together they have expanded the volume of Community Law. This development, in some quarters, has been regarded as excessive and petty regimentation. However, whether controlling additives to food products, defining honey, quality of fruit juices, bathing water, or insisting on safety standards for motor vehicles, control of exhaust fumes and rear-view mirrors, the harmonization program has contributed

to the improvement of standards and the elimination of unfair competition by shoddy goods in the Community.'[37]

Also of importance to European business is the Community's harmonization of certain areas of national substantive law. These on-going alignments draw their legitimacy from several EEC Treaty provisions[38] which read together evince a broad power, a power which has been manifested in the form of directives, regulations and, in some cases, conventions.[39]

The company law harmonization program in particular is illustrative of the extent to which legal integration will be reflected in fundamental business operations. The EEC Treaty addresses company law specifically in the context of the Treaty's pre-occupation with the free movement of persons, services, and capital. In order that corporations shall enjoy freedom of establishment and the right to non-discrimination on grounds of nationality, Member States are required, subject to certain safeguard measures, to effect a progressive abolition of restrictions and to refrain from introducing new restrictions.[40]

The Community has a corresponding obligation to co-ordinate 'to the necessary extent the safeguards which, for the protection of the interests of members and others, are required by Member States of companies or firms . . . with a view to making such safeguards equivalent throughout the Community'.[41] The description 'companies or firms' is intended to be widely embracive, and thus includes enterprises or undertakings notwithstanding their technical appellation. Omitted, however, are non-profit making entities.

The execution of the Treaty's mandate to co-ordinate safeguards required of companies has thus far resulted in one convention and several directives, accepted and draft. The former addresses the Mutual Recognition of Companies and Bodies Corporate.[42] Its basic thrust is to extend to entities incorporated in, and having a registered office in, one of the Member States the capacity to bear corporate rights and duties within the signatory states.

Under the Convention, a recognized entity, subject to some important limitations,[43] is to be accorded in one Member State the capacity granted to it by the law of the Member State under which it has been established. Recognition is not accorded to entities having their central administration outside the convention territories absent some substantial link with such territories or provision to them of freedom of establishment by virtue of a trade agreement between the EEC and the country under whose laws they exist.

Safeguard provisions do exist under which a Member State may limit the effects of recognition in light of its so-called 'imperative' rules of its domestic law. The scope of this prerogative remains subject to some debate, thus engendering some conservatism on the part of companies exercising their right of recognition. For example: may a company established under German law but having its actual administration in France be penalized for making a loan to its directors where such loans are within its power under German law but absolutely prohibited under French Company law? The answer remains unclear.[44]

Other limitations concern the signatory state's ability to refuse to apply the Convention where to do so would derogate 'public policy' as defined by its Private International (Conflicts) Law.[45] Such rules of public policy have not been codified in the Community. Some measure of flexibility is therefore afforded Member States. Rules or principles which contravene the EEC Treaty, however, may not qualify as justifying 'public policy'.[46] The supremacy of EEC law therefore serves to moderate a Member State's ability to exploit the public policy exception in its treatment of entities formed under the laws of other Member States.

As will readily be appreciated, the recognition of companies likely will infringe fewer national interests to the extent that the company laws of Member States are aligned. Such is the role of the series of directives on company law. Demonstrating what company law in Europe is becoming, the scope and substance of these deserve attention by those seeking a familiarity with corporate law within the Community. Business entities operating under the laws of a Member State increasingly will be subject to national regulation introduced in compliance with the existing five directives and their successors. The substantive areas presently affected are highlighted by the following selective summary:

(1) *Protection of shareholders, creditors, and the public through disclosure.* Section 1 of the First Directive[47] as augmented by the Fourth Directive[48] exhort Member States' legislatures to require of public companies and certain large private companies the disclosure and/or publication in the relevant register of such documents and details as the company statutes and amendments thereto, information about company officers and their role in management, capital and annual accounts, transfers of the company's domicile, declarations of company nullity, the initiation of winding-up proceedings and the appointment of liquidators.

(2) *Protection of third parties, limiting the ultra vires and constructive notice doctrines.* The First Directive also provides that, where company officers act within the powers allowed to be given them by national law, the fact that their powers are restricted by a shareholders' meeting or provisions of the company statutes cannot alone relieve the company of obligations otherwise created. Absent something more than constructive knowledge by the third party, the company remains bound. The effect of such internal limitations on an officer's authority may, however, in a given Member State, be the creation of personal liability on the part of the officer for losses sustained by the corporation through such *ultra vires* acts. A third section limits and defines the circumstances under which a company can be declared a nullity.

(3) *Company formation – creation and maintenance of capital.* Larger, public-type, European companies such as the French *Société Anonyme,* the German *Aktiengesellschaft,* or the English Public Limited Company are subject under the Second Directive[49] to minimum capital requirements, restrictions on the source of dividends and the circumstances under which a company may repurchase its own shares. As with most areas touched by the company law harmonization program, the pre-directive national laws in this area demonstrate

significant variations, particularly when comparing the common law with the civil law systems included among the ten.

(4) *Mergers of 'public' companies – shareholder and employee apprisal – Third Directive.*[50] Where entities of the class covered by the First and Second Directive seek to merge, either by absorption of one company by another or by the creation of a third company, Member States have been directed to provide, *inter alia,* for shareholder approval of a merger plan which must set forth details relative to share capital transfer terms, and certain technical aspects of the scheme. Consistent with the communities' emphasis on employee participation, employees' representatives are entitled to address the relevant shareholders' meeting.

(5) *Management structure – employee participation.* The controversial Fifth Directive[51] remains in Draft Form. The present version would have Member States require of public companies a two-tier management structure comprising a management organ overseen by a supervisory organ. In companies employing more than 500 persons, the supervising organ would include members, one-third of which have been appointed by employees, or would require employee approval. The supervising organ would have the power to appoint and dismiss management. Further, management would, regarding certain major decisions affecting the company, be obliged to obtain authorization from the supervisory body. Shareholder interests are protected in part by detailed provisions which seek to ensure a regular and informed shareholders' meeting.

(6) *Other company law areas being harmonized.* The Draft Sixth,[52] Seventh, and Eighth Directives regard the contents of prospecti, the format of consolidated accounts, and the qualifications of statutory auditors respectively.

Other branches of substantive law being harmonized. The development of economic union through the harmonisation of the substantive law of Member States has extended to several other areas which will affect business. These include:

(1) Patents and Trademarks – the former has to an extent been harmonised by conventions[53] and a recent draft regulation produced by the Commission suggests further developments regarding the interface between patent licensing and Community competition law.[54] Trademarks are the subject of a draft convention[55] concerning which work will continue through the mid–1980s.

(2) Banking Law – though insurance institutions are covered to a large extent by the company law harmonisation program, credit institutions are slated to receive separate treatment. A first directive[56] sets forth a uniform procedure and set of standards which, when adhered to, create a right of establishment and the freedom to provide services in the EEC.

(3) Investment Law – gradually, stock exchange and investment activity is becoming subject to uniform requirements. Conditions for admission of securities to an official stock exchange listing, listing particulars, mutual fund law, transferable company securities admitted to official stock exchange listings, regulation of stockbrokers and insider trading are

subjects which are dealt with or which have been proposed as draft directives.[57]

(4) Bankruptcy – first published in 1970, the Draft Convention[58] in this area is expected to achieve completion in the early 1980s.

(5) Taxation – a uniform tax system is beyond the aims of the Common Market but in order to facilitate cross-frontier commerce and to create a direct and independent source of revenue, the EEC has embarked on a limited harmonisation of the tax field. The adoption of a value added tax (VAT) represents the major focus of the program. The tax which is levied at each stage of production and distribution, after certain deductions, has been instituted through the use of several Directives.[59] Entities transacting business in Europe to greater or lesser extent will no doubt become familiar with the elaborate scheme the VAT implies. Other measures influencing taxation are numerous[60] and include a Directive addressing company taxation and witholding taxes on dividends.[61]

European competition law. A wide range of Community policies may affect business in Western Europe. In addition to those basic to the Customs Union and Common Commercial Policy, several others can be identified: competition, industrial, unions and social, energy, economic and monetary, regional, technological and research and development, environmental, political co-operation, agricultural, transport, financial and fiscal, and consumer. While it is beyond the ambition of this introduction to treat the aforementioned régimes in detail,[62] because of its potential impact on business planning the Community's regulation of competition warrants special attention by entities contemplating operations in Western Europe. The point is best served perhaps by noting that abridgement of Articles 85 and 86 can lead not only to the non-enforceability of an agreement otherwise flawless under national law, but also to substantial fines.[63]

The principal objectives of the Community's competition policy have been summarised as follows: to create a single market for the benefit of industry and consumers by preventing undertakings from hindering the free flow of goods through the use of restrictive agreements and cartels; to prevent the abuse of economic power; and to encourage companies through continuing commercial rivalry to rationalize and change with progress, thus keeping pace with world markets.[64] Issues relative to the competition laws of the Community can arise in many contexts. A typical scenario would involve one party to a contract raising Article 85 as a defense to a breach of contract action brought in the national court of a Member State. The courts of Member States are obliged not to give effect to agreements falling within Article 85(1).[65] In some European countries, infringement of Article 85 may lead to tort liability.

The Treaty chapter devoted to Rules on Competition includes Articles 85–90. The pillars of this regime are Articles 85 and 86 as reinforced by certain secondary legislation. The wording of these articles follows:

Article 85

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of