



INSIGHT

IMPACT OF *BREXIT* ON EUROPEAN COMPANY LAW: A FRENCH PRIVATE INTERNATIONAL LAWYER PERSPECTIVE

JEREMY HEYMANN*

ABSTRACT: Although the outcome of the Brexit remains quite uncertain, this *Insight* aims at contemplating, from a private international law perspective, what the consequences of *Brexit*, in the field of Company law, could be. From Incorporation to (possible) freedom of movement, through recognition (and its consequences), the major steps of corporate life are here analyzed through *Brexit*. Oddly enough, the impact of Britain's EU withdrawal in the corporate field could be, under many aspects, not as major as feared.

KEYWORDS: company law – right of establishment – Brexit – freedom of movement – recognition – applicable law.

I. INTRODUCTION

Hard *Brexit*? Soft *Brexit*? Like the political one, the legal forecast is quite blurry, at least unclear, and therefore subject to change. Confronted to such a – moving – work in progress, the uncertainty seems now to be in order. Thus, some can even think (dream?) about a never ending transitory period, or even a never coming *Brexit*.¹ Of course, one can always recall the famous quote, according to which the Parliament of the United Kingdom (hereinafter “UK”) “can do everything, except making a woman a man, or a man a woman”.²

Almost anything could happen, then. But some facts are nonetheless – as for now –, certain. A Bill to Repeal the European Communities Act 1972 and make other provision in connection with the withdrawal of the United Kingdom from the EU has been read

* Professor of Law, Lumière Lyon 2 University, jeremy.heyman@univ-lyon2.fr.

¹ See e.g. N. CLEGG, *How to Stop Brexit (and Make Britain Great Again)*, London: Penguin Books, 2017.

² J.-L. DE LOLME, *The Constitution of England; Or, an Account of the English Government; in Which it is Compared both with the Republican Form of Government, and the Other Monarchies in Europe*, London: G. Wilkie & J. Robinson, 1807, p. 132, *ad notam*: “[...] for it is a fundamental principle with the English lawyers, that parliament can do everything, except making a woman a man, or a man a woman”.

for the first time in the House of Commons on 13 July 2017,³ and such a Bill followed the activation of Art. 50 TEU by the UK Government,⁴ *i.e.* a provision which permits a Member State to notify its intention to leave the EU on the condition that constitutional requirements have been fulfilled.⁵

Although the outcome remains blurry, and while the negotiations between the European Union and the United Kingdom are not yet over, it appears nevertheless that the TEU and the TFEU will, sooner or later, cease to produce their legal effects in UK. Being a first, this kind of secession will reshape, for better or worse, the relationship between UK and EU.

In the particular field of European Company law, such a reshaping would induce a certain number of consequences, which the present study is intending to highlight. To envisage all the legal consequences of the aforementioned secession being attempting the impossible, we will restrict our focus on chosen specific points, in relation with the right of establishment, and obviously from the sole EU law perspective. Namely, only the incorporation (II) and the recognition processes (III), as well as the freedom of movement of UK (and especially England)/other Member States companies (IV), because of their great practical importance, will be scrutinized below.

II. INCORPORATION

As it is nowadays well known, Art. 49, para. 2, TFEU provides that “[f]reedom of establishment shall include the right [...] to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is effected [...]”.

Until now, this provision has thus allowed all citizens of the EU to move freely from any Member State to UK, and to invoke there subsequently the right to set up and manage undertakings. Such a right of establishment could not be hampered nor denied, as “restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. [Furthermore,] [s]uch prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State”.⁶ Consequently, at least for what regards companies and subsidiaries, the right of

³ UK House of Commons, European Union (Withdrawal) Bill (HC Bill 5) 2017-19, 13 July 2017.

⁴ Art. 50, para. 1, TEU provides that “[a]ny Member State may decide to withdraw from the Union in accordance with its own constitutional requirements”.

⁵ See Art. 50, para. 2, TEU, and the UK Supreme Court judgment of appeal of 24 January 2017 *R (Miller) v. The Secretary of State for Exiting the European Union* (Rev 3), [2017] UKSC 5. See also the so-called “Three Knights Opinion”, rendered on 10 February 2017 by Sir David Edward KCMG PC QC, Sir Francis Jacobs KCMG PC QC, Sir Jeremy Lever KCMG QC, Helen Mountfield QC and Gerry Facenna QC.

⁶ Art. 49, para. 1, TFEU.

establishment granted by Art. 49 TFEU must be considered as offering access to incorporation in the UK to any EU citizen, as well as a concomitant choice of applicable law to the company/subsidiary. Indeed, as the ECJ observed, “companies are creatures of national law and exist only by virtue of the national legislation which determines its incorporation and functioning”.⁷ Hence, any citizen of the EU using his/her freedom of movement to go to the UK to set up and manage an undertaking was – and still is – implicitly but surely making a choice of the law that would apply to this undertaking.

Defined as a “very broad one”,⁸ the concept of establishment has been considered by the Court of Justice since 1995 as “allowing a Community national to participate, on a stable and continuous basis, in the economic life of a Member State other than his State of origin and to profit therefrom, so contributing to economic and social interpenetration within the [European Union]”.⁹ After *Brexit*, the right to such an establishment should no longer be granted to citizens of the EU moving to UK. Therefore, UK law (and especially English law), at least in theory, could quite be reshaped in order to strengthen the conditions imposed to foreigners, including all EU citizens, to access incorporation in UK. Such an outcome seems however quite hypothetical, as it is hardly realistic to consider that post-*Brexit* UK would cease to be less business-friendly as it is now. On the contrary, it is almost certain that UK law (and especially English law) won’t evolve, i.e. that it would keep on offering the current access conditions to incorporation to newcomers. Or perhaps it would evolve, but accordingly, only to adapt in order to become even more business-friendly, and search for new means to appear even more attractive than it is considered to be now.

Be that as it may, on the other shores of the Channel, i.e. within all Continental Europe, a slightly different approach would/could certainly be preferred. Indeed, no Member State save for UK and Ireland would probably have forgotten the path that the *Centros* judgment opened in the field of interstate exercise of a business activity.¹⁰ But this is already raising the question of recognition and its consequences.

III. RECOGNITION (AND ITS CONSEQUENCES)

According to Art. 54 TFEU, “[c]ompanies formed in accordance with the law of a Member State and having their registered office, central administration or principal place of

⁷ Court of Justice, judgment of 27 September 1988, case C-81/87, *The Queen v. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust PLC*, para. 19.

⁸ Court of Justice, judgment of 30 November 1995, case C-55/94, *Gebhard v. Consiglio dell’Ordine degli Avvocati e Procuratori di Milano*.

⁹ *Ibid.*, para. 25. See also Court of Justice, judgment of 23 February 2016, case C-179/14, *European Commission v. Hungary* [GC], para. 148; judgment of 21 December 2016, case C-201/15, *Anonymi Geniki Etairia Tsimenton Iraklis (AGET Iraklis)* [GC], para. 51. See however Court of Justice, judgment of 25 October 2017, case C-106/16, *Polbud – Wykonawstwo* [GC], paras 38-44.

¹⁰ Court of Justice, judgment of 9 March 1999, case C-212/97, *Centros*.

business within the Union shall [...] be treated in the same way as natural persons who are nationals of Member States". Besides assimilating legal persons to natural persons, this provision is granting companies the benefit of national treatment wherever they wish to exercise their business activity. Of great practical importance, such a principle of national treatment is aiming at protecting companies not to be discriminated, *i.e.* not to be treated less favorably in any Member State other than the one where they have their registered office, central administration or principal place of business.

However, when a company has only been formed in accordance with the law of a Member State (that promotes a very liberal company law), in order to exercise its whole business activity in another Member State by means of a branch, could that former State refuse to register this branch, and by doing so, refuse to recognize the company which has yet been formed in accordance with the latter State? In other words, can Member States fight the so-called letterbox entities' phenomenon?

Since the Court of Justice's *Centros* judgment,¹¹ the answer to such a question is negative. The Court indeed considered – and still considers – that "[t]he right to form a company in accordance with the law of a Member State and to set up branches in other Member States is inherent in the exercise, in a single market, of the freedom of establishment guaranteed by the Treaty".¹² Of course, it has all the same been admitted that "a Member State is entitled to take measures designed to prevent certain of its nationals from attempting, under cover of the rights created by the Treaty, improperly to circumvent their national legislation or to prevent individuals from improperly or fraudulently taking advantage of provisions of [EU] law".¹³ However, as it has been ruled that "the fact that a national of a Member State who wishes to set up a company chooses to form it in the Member State whose rules of company law seem to him the least restrictive and to set up branches in other Member States cannot, in itself, constitute an abuse of the right of establishment",¹⁴ it has quickly become clear for Member States that they could not, under EU primary law, legally fight the letterbox entities' phenomenon. As a result, the number of companies registered in the UK, and having their head offices in other Member states, exploded.¹⁵

¹¹ *Ibidem*.

¹² *Ibidem*, para. 27.

¹³ *Ibidem*, para. 24.

¹⁴ *Ibidem*, para. 27.

¹⁵ According to the Impact assessment SEC(2007) 1707 of 12 December 2007 from the Commission on the Directive on the cross-border transfer of registered office, those companies were around 20.000 in 2005, *i.e.* "5 times more than in 2001, before the relevant judgments of the Court of Justice were delivered" (*ibid.*, p. 11), namely the *Überseering* (Court of Justice, judgment of 5 November 2002, case C-208/00, *Überseering*) and *Inspire Art Ltd* (Court of Justice, judgment of 30 September 2003, case C-167/01, *Inspire Art Ltd*) judgments.

The Court's *Inspire Art Ltd* judgment provides another good example.¹⁶ When confronted with a situation that is similar to the one of the *Centros* case, can the host Member State impose its international mandatory rules on the company that intends to carry on its entire business in the State in which its branch is to be set up?¹⁷ It is well known nowadays that the Court also answered negatively to such a preliminary question.¹⁸ The line of argument developed by the Dutch Government was yet convincing, as it invited the Court to take into account that, contrary to the refusal of the Danish Trade and Companies Board to register a branch of a company formed in accordance with the legislation of another Member State – which led to the refusal of recognition of the *Centros* company – in the *Centros* case, the Dutch Chamber of Commerce considered in the case before the Court that only a statement should be added to the company's registration in the commercial register, namely that *Inspire Art Ltd* was formally a foreign company (*formeel buitenlandse vennootschap*), with the result that some provisions of Dutch company law could apply as *lois de police*.¹⁹

As a result of the above, it appears that the *Centros* and the *Inspire Art Ltd* cases look like fraternal twins.²⁰ Indeed, the particularity of the *Inspire Art Ltd* case is that Dutch authorities, although they wanted to impose on the company several international mandatory provisions of Dutch company law, nevertheless recognized the legal personality of the company established in the United Kingdom.

Having said that, it remains that for the time being, the fact that a company carries on its activities exclusively or almost exclusively in the Member State of its secondary establishment does not deprive it of the right to invoke the freedom of establishment guaranteed by the TFEU. However, what would/could happen after *Brexit*?

¹⁶ *Inspire Art Ltd*, cit.

¹⁷ Compare with Supreme Court of Delaware, judgment of 16 September 1987, 531 A.2d 206, *McDermott Inc. v. Lewis*, with regard to the “internal affairs” rule. See also US Supreme Court, judgment of December Term, 1868, 75 U.S. (8 Wall.) 168, *Paul v. Virginia*, para.181.

¹⁸ The Court of Justice ruled that the relevant provisions of the EC Treaty (now TFEU) “preclude national legislation [...] which imposes on the exercise of freedom of secondary establishment in [a] State by a company formed in accordance with the law of another Member State certain conditions provided for in domestic law in respect of company formation relating to minimum capital and directors’ liability”, *Inspire Art Ltd*, cit., para. 105.

¹⁹ Compare with the outreach statutes adopted in the United States, notably in the States of New York and California (see *New York Business Corporation Laws*, in McKinney, 1986, para. 1320; *California Corporation Code*, in West, 1977 & Supp., 1989, para. 2115). See also US Supreme Court, judgment of 23 June 1982, *Edgar v. MITE Corp* and judgment of 21 April 1987, *CTS Corp. v. Dynamics Corp. of America*, para. 90, where the US Supreme Court ruled that the “free market system depends at its core upon the fact that a corporation – *except in the rarest situations* – is organized under, and governed by, the law of a single jurisdiction, traditionally the corporate law of the State of its incorporation” (emphasis added).

²⁰ On this comparison, see already J. HEYMANN, *The Relationship Between EU Law and Private International Law Revisited: Of Diagonal Conflicts and the Means to Resolve Them*, in *Yearbook of Private International Law*, 2011, p. 574 *et seq.*

Although it is almost certain that Member States would keep on recognizing the companies formed in accordance with UK law,²¹ it is yet unlikely that they would keep on following Court of Justice's case-law relating to the interstate exercise of a business activity.²² Once the United Kingdom will no longer be a Member State, no provision of the TFEU could certainly prevent the Member States to apply some of their provisions as international mandatory rules, especially in cases similar to the *Centros* and *Inspire Art Ltd* ones. There is thus a real risk for UK (and especially England) to cease being an attractive country for private limited companies wishing to operate their business from another (Member) State, and to watch in the meanwhile another country becoming for this type of companies some sort of new Eldorado. Another serious risk would be for United Kingdom (and especially for England) to observe a "rush" of its companies outside the country by the means of transfer of the head office. This is typically what the freedom of movement of companies deals with.

IV. FREEDOM OF MOVEMENT

Unlike the interstate exercise of a business activity, the interstate/international transfer of a seat raises primarily a query relating to the retention of legal personality. As Bartin, in France, first put it, such a transfer creates in fact a *conflict mobile*, i.e. changes in the connecting facts.²³ Given that the governing law of a company is usually the law of the State where the head office has been fixed, the transfer of the former into another State would in most cases result in an alteration of the law applicable to the company.

Classically, this kind of conflict is solved by a distributive applicability of the relevant laws, namely the one of the State of departure and the one of the host State. However,

²¹ From 1857 to 2007, France has enacted a specific legislation that provided that foreign corporations could not sue in French courts unless authorized to do so by decree. Bilateral treaties used to make that provision inoperative, but some foreign corporations – i.e. corporations that were incorporated in countries that had not signed such bilateral agreements – nonetheless found themselves barred in France. However, since the first era of globalization in early 1990s, French courts ruled repeatedly that the French Act of 30 May 1857 was contrary to the provisions of the European Convention for the Protection of Human Rights and Fundamental Freedoms (Arts 1, 14 and 6, para.1) and its first additional Protocol (Arts 1 and 5). See e.g. French Court of Cassation, judgment of 8 July 2003, no. 00-21.591. Since such an Act has been abrogated by the Simplification of the Law Act of 20 December 2007 (Law no. 2007-1787 of 20 December 2007 (France), p. 20639), it is very unlikely that France – or any other Member State – will not, post-*Brexit*, recognize companies incorporated in UK. Besides, the fact that all economies are nowadays intertwined advocates in this sense.

²² See e.g. the two different paths that Germany followed when confronted to cases where the application of its *Sitztheorie* was at stake: recognition or "recharacterization", depending on whether the foreign company was incorporated in a Member State or in a third State (for further details, see notably P. KINDLER, *Internationales Gesellschaftsrecht 2009: MoMig, Trabrennbahn, Cartesio und die Folgen*, in *IPRax*, 2009, p. 189 *et seq.*)

²³ É. BARTIN, *Principes de droit international privé selon la loi et la jurisprudence françaises*, Paris: Domat-Montchrestien, 1930-1935, p. 193 *et seq.*, para. 78.

and although such a traditional solution leaves the liberty that is given to Member States to choose the connecting factor that will designate the applicable law to companies unrestrained, it follows from the case-law of the Court of Justice that it may be clashing with the freedom of movement enshrined in the TFEU. Indeed, any “barrier to the actual conversion of [...] a company, without prior winding-up or liquidation, into a company governed by the law of the Member State to which it wishes to relocate constitutes a restriction on the freedom of establishment of the company concerned which, unless it serves overriding requirements in the public interest, is prohibited under [EU law]”,²⁴ the principle being “that company transformation operations are [...] amongst those economic activities in respect of which Member States are required to comply with the freedom of establishment”.²⁵

Consequently, and in other words, whether the sought conversion results from a merger²⁶ or a transfer of a head office, it has been held that “the company concerned enjoys a right granted by the European Union legal order [...], the right to carry out a cross-border conversion”.²⁷

In a post-*Brexit* era, such a right to carry out a cross-border conversion would no longer be granted to companies wishing to relocate either in the UK (departing from a Member State) or in a Member State (departing from UK).

As for the States, such a consequence would make them come back to the state of applicable law at the time when the *Daily Mail* judgment was delivered,²⁸ i.e. a time when it was acknowledged that “the differences in national legislation concerning the required connecting factor and the question whether and if so how the registered office or real head office of a company incorporated under national law may be transferred from one Member State to another [State] as problems which are not resolved by the rules concerning the right of establishment but must be dealt with by [...] conventions”.²⁹ The UK as well as the Member States would thus be enjoying their once full liberty in that field, and they would be able to unilaterally decide whether a company incorporated on their soil, i.e. whether their “creature” may or may not leave their territory to carry out a cross-border conversion. In other words, the States would recover in such an era their right to life and death upon their legal persons.

It is however unclear whether it would be seen as a decline or a renewal. But it would certainly render such cross-border operations uneasy to perform, and, truth be told, in-

²⁴ Court of Justice, judgment of 16 December 2008, case C-210/06, *Cartesio* [GC], para. 113.

²⁵ Court of Justice, judgment of 12 July 2012, case C-378/10, *VALE Épitési*, para. 24. See also judgment of 25 October 2017, case C-106/16, *Polbud – Wykonawstwo* [GC], paras 38-44.

²⁶ Court of Justice, judgment of 13 December 2005, case C-411/03, *Sevic Systems AG* [GC].

²⁷ *Ibid.*, para. 49.

²⁸ *The Queen v. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust PLC*, cit.

²⁹ *Ibid.*, para. 24.

opportune. Why indeed risk that the State of departure would require the winding-up or liquidation of the company that intends to reorganize itself in another State? Such a perspective would certainly lead the operators wishing to carry out a cross-border conversion to contemplate the possibility of resorting to the carve-out (or spin-off) of their activities, whilst keeping the original registered office of the company in the UK.

The creation of a subsidiary in one of the Member States could thus be used for this purpose. Such a creation would practically seek to make the newly incorporated company benefit from the right of establishment enshrined in Art. 49 TFEU, and from the case law based on it. However, if one recalls the General Programme for the abolition of restrictions on freedom of establishment as adopted by the former Council of the EEC,³⁰ companies and firm “who wish to set up [...] subsidiaries in a Member State” are “entitled to benefit from the abolition of restrictions on freedom of establishment as set out in this General Programme [...] provided that, where only the seat prescribed by their statutes is situated within the Community [...], their activity shows a *real and continuous link* with the economy of a Member State”.³¹ Furthermore, the General Programme provides that “such link shall not be one of nationality, whether of the members of the company or firm, or the persons holding managerial or supervisory posts therein, or of the holders of the capital”.³²

In other words, the resort to a subsidiary as a way to access the EU market implies carrying out a genuine economic activity in the territory of the host Member State. It is indeed understood that the setting-up of a subsidiary as a stalking horse will be regarded as having the characteristics of a “wholly artificial arrangement”,³³ as no “‘front’ subsidiary” can be tolerated within the EU.³⁴

V. CONCLUSION

Having reached the end of this study, it appears that the legal forecast is certainly quite blurry. What will be the outcome of *Brexit* in the field of European Company law? This study has sought to suggest what could happen, in relation with incorporation, recognition, or freedom of movement of companies. Many questions remain yet unanswered: will a new era begin? Will there be something good coming out of it? Will the lawyers be

³⁰ General Programme of the Council of the EEC of 18 December 1961 for the abolition of restrictions on freedom of establishment, p. 36.

³¹ *Ibidem*. Emphasis added.

³² *Ibidem*.

³³ Court of Justice, judgment of 12 September 2006, case C-196/04, *Cadbury Schweppes and Cadbury Schweppes Overseas* [GC], para. 68.

³⁴ *Ibidem*.

so creative as to prove Giraudoux right, when he wrote, “we all know here that the law is the most powerful of schools for the imagination”?³⁵

Maybe the general conclusion could be more realistic, in Hemingway’s style: “This was a big storm and he might as well enjoy it. It was ruining everything, but you might as well enjoy it”.³⁶

³⁵ J. GIRAUDOUX, *Théâtre complet*, Préface de J.-P. GIRAUDOUX, Paris: Gallimard, 1982, p. 522, *La Guerre de Troie n’aura pas lieu* (Acte II, Scène V) (free translation).

³⁶ E. HEMINGWAY, *For Whom the Bell Tolls*, London: Arrow, 2004, p. 189.

