THE COMPANY LAW HARMONIZATION PROGRAM OF THE EUROPEAN COMMUNITY

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The company law harmonization program is, according to its proponents, a comprehensive attempt by the European Community to protect employees, shareholders, and the public against certain kinds of corporate misconduct. The program consists of legislation aimed at harmonizing, throughout the Member States of the EC, certain aspects of corporate operations including capitalization, public offerings, disclosure, mergers, and consultations with employees. It would affect EC companies as well as non-European companies with subsidiaries located in EC Member States. The author discusses this legislation along with the Vredeling Proposal, a controversial proposed EC directive that would require management to disclose information to and consult with workers' representatives, and a model corporate charter for the Societas Europea. The author believes that although the harmonization proposals already in operation as well as those currently under consideration suffer from certain serious deficiencies, and that although they have been greeted by a somewhat hostile, retaliatory reaction in the United States, the European program is likely to continue. Therefore, he urges that U.S. policymakers adopt a broad-based approach to resolving differences of opinion with the EC, and that there be greater willingness to cooperate on both sides: while Europeans need to recognize that creating an atmosphere hostile to non-European business could undermine the beneficial effects of the harmonization program, it is time that non-Europeans, and especially U.S. businesses, become aware of the important economic, political, and social objectives that underlie the EC program.

For most non-Europeans, the establishment and evolution of the

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European Community (EC)[1] have been no more than subjects of academic interest. Many have noted with genuine satisfaction the growing interdependence of the ten Member States of the EC,[2] nations whose cultures, languages, and histories differ widely and fundamentally. The forging of a true economic union of nations which, within the lifetimes of their leaders, have fought two World Wars is little short of a miracle.[3] Nevertheless, few non-Europeans, including those with significant business interests in Europe, have heeded the emergence of a comprehensive and increasingly complex EC legal order.[4] Recent proposed EC legislation affecting companies located in or with subsidiaries located in Member countries has, however, caused many executives of U.S. multinational corporations to consider the impact of the EC's efforts on their activities. Many U.S. businesses have begun crash-courses in EC law and politics in order to counter what they perceive to be serious threats to their methods of operation in Europe and, ultimately, in

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1. Treaty establishing the European Economic Community, *done* Mar.25,1957, art. 85, 298 U.N.T.S 3 [hereinafter cited as Treaty of Rome]. This article uses the term "European Community" or "EC" in accordance with the resolution of the European Parliament urging the adoption of that nomenclature. Resolution of February 16, 1978, 21 O.J. EUR. COMM. (No. C 63) 36 (1978). In July, 1967, the substantive duties of the three Commissions of the "Common Market"—the European Economic Community (EEC), the European Atomic Energy Community (EURATOM), and the European Coal and Steel Community (ECSC)—were combined and vested in the newly created Commission of the European Communities. Treaty Instituting a Single Council and a Single Commission of the European Community, Apr. 8, 1965, art. 9, 10 O.J. EUR COMM. (No. C 152) 2 (1967) [hereinafter cited as Merger Treaty]. For all practical purposes, the three Communities now share all of their institutions and have become a single entity.

2. The six original Member States were Belgium, the Federal Republic of Germany, France, Italy, Luxembourg, and The Netherlands. Treaty of Rome, *supra* note 1, arts. 1-3. On January 1, 1973, Denmark, the Republic of Ireland, and the United Kingdom joined the Community. Greece became the tenth member on January 1, 1981. Lewis, *The Nine Becomes Ten,* N.Y. Times, Feb. 8, 1981, at A29, col. 3. Spain and Portugal are scheduled to join in 1984 or 1985. ECONOMIST, Aug. 22, 1980, at 41; BUS. AM., Nov. 3, 1980, at 22.

3. The true economic union, however, has recently shown signs of internal dissension. Greenland has become the only territory within the EC to vote to secede, Pederson, *Withdrawal from the EC Voted by Greenland,* Wall St. J., Feb. 25, 1982, at 30, col. 3, and the United Kingdom and Greece have expressed doubts about continuing their membership. Lewis, *Common Market Facing Crisis over British Issue,* N.Y. Times, May 13, 1980, at A2, col. 3; Ashby, *Greece Unlikely to Withdraw: Issue May Be Decided by Electorate, Not Govt.,* Am. Banker, Dec. 16, 1981, at 10.

4. There is one notable exception to this generalization: the development of EC antitrust law, pursuant to the Treaty of Rome, *supra* note 1, arts. 85, 86, has received considerable at-

the United States as well.[5]

This article will discuss proposed legislation among EC Member States to encourage the "harmonization" of certain diverse aspects of corporate operations, including disclosure of information, capitalization, mergers, public offerings of securities, qualifications of auditors, relationships within "groups" of companies, and consultations with employees. After outlining the concept of harmonization and the procedure for its attainment, the article will review EC initiatives which have already been promulgated, which are in the process of being adopted, and which have not yet been formally proposed, and will indicate those aspects of the program which should especially concern U.S. industry. Although not strictly part of the company law harmonization program, the Vredeling Proposal, a proposed directive requiring that management disclose certain information to and consult with workers' representatives, and a model corporate charter for the Societas Europea are also discussed. Finally, the concluding section will present a critique of the harmonization program together with an assessment of its current status and prospects, and will suggest resolutions to some of the most frequently disputed issues it raises.

THE CONCEPT OF HARMONIZATION

One essential aspect of the European Community's goal to permit the free movement of persons, services, and capital among Member States is what the Treaty of Rome terms "the right of establishment."[6] This right comprises, inter alia, the freedom of a

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tention in this country. *See, e.g.*, HAWK, UNITED STATES, COMMON MARKET, AND INTERNATIONAL ANTITRUST: A COMPARATIVE GUIDE chs. 7-13 (1981).

5. The National Foreign Trade Council (NFTC), representing more than 650 companies from its headquarters in New York, established a Europe Committee in early 1980. Whyte, *Foreign Trade Council Moves to the Capital,* BUS. AM., Nov. 16, 1981, at 11. The American European Community Association was founded later that year. Farnsworth, *More Bridgebuilding,* N.Y. Times, Dec. 7, 1981, at D2, col. 3.

6. Treaty of Rome, *supra* note 1, arts. 52-58. The Legal Service of the Executives of the Communities stated:

> The benefit of the right to create establishments of secondary nature cannot be made subject to prior coordination. The authors of the Treaty were fully aware that the Company Laws in Member States were far from uniform but they accepted the inherent difficulties because they thought that the scope of the right of establishment would be substantially reduced if it were limited to physical persons

national company of any Member State to establish or maintain a business in any of the other Member States.[7] To enable EC institutions to realize the freedom of establishment, the Treaty of Rome grants them power to "coordinat[e] 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."[8] The program of company law harmonization has been constructed on this foundation.[9] The principal component concepts of harmonization—coordination, safeguards, protection, and equivalence—are immediately apparent in this enabling language. Legislation of Member States designed to protect shareholders and "others," (presumably creditors, customers, potential investors, and workers) by reducing their exposure to unacceptable risk is to be harmonized throughout the EC.

In order to attain harmonization, the Treaty of Rome gives the EC Council of Ministers the power to issue directives to the Member States.[10] A directive is not legislation per se; rather, it is an order issued by the Council to Member States requiring that they bring their national legislation into conformity with the directive. A directive is binding "as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national

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only clearly inconvenienced. The difference in the Company Laws might arise from differences in rules concerning access to non-salaried activities generally. This is why the Treaty, in addition to suppressing discrimination, provided for coordination both of national provisions for access to non-wage earning activities (art. 57) and of certain limited aspects of the Company Laws (art. 54, para. 3(g)).

6 2 JURCEE, June 21, 1962, at 1509.

7. Treaty of Rome, *supra* note 1, art. 52.

8. *Id.* art. 54, para. 3(g). Perhaps the most immediate consideration behind this provision was that Member States would find it difficult to remove the traditional restrictions or special formalities imposed upon foreign companies and to admit and treat them as domestic companies unless they met certain standards with respect to the protection of their creditors and shareholders. Jepson, *Die Genehmigung des Gewerbetriebs ausland ist der juristischer Personum in der Bundesrepublik Deutschland,* 1966 AUSSENWIRTSCHAFTASDIENST DES BETRIEBS-BERATERS 21.

9. "The purpose of the European company law, whatever form it may take, is to remove or reduce the obstacles to transnational commerce and economic coalescence, which derive from the coexistence of separate and more or less divergant national legal systems within the legal order of the Community." STEIN, HARMONIZATION OF EUROPEAN COMPANY LAWS: NATIONAL REFORM AND TRANSNATIONAL COORDINATION (1971).

10. Treaty of Rome, *supra* note 1, art. 54(2) states:

authorities the choice of form and methods."[11] Thus, harmonization does not necessarily apply the law of any one Member State directly to the European Community at large.[12]

The process by which the Council adopts directives is complex. The Commission of the EC, which is, in essence, the civil service of the Community, and which is composed of members who, with their staffs, do not represent their individual countries, is responsible for proposing draft directives to the Council.[13] On all proposed directives, the Council must seek the advice of the European Parliament,[14] and of the Economic and Social Committee (ECOSOC) if the proposal concerns matters within its purview.[15] Any changes in the text suggested by Parliament or ECOSOC must be duly considered by the Commission. The Commission normally responds to these suggestions in writing, whether or not it elects to make the suggested revisions.[16]

> In order to implement this general programme, or in the absence of such programme, in order to achieve a stage in attaining freedom of establishment as regards a particular activity, the Council shall, on a proposal from the Commission and after consulting the Economic and Social Committee and the [Parliament] issue directives, acting . . . by a qualified majority.

Id.

11. *Id.* art. 189. By contrast, a "regulation" is of direct effect and is legally binding in its entirety. *Id.* Verbond Van Nederlandes Ondernemingen v. Inspecteur der Invoerrechten en Accijnzen, 1977 E. Comm. Ct. J. Rep. 113, 1977 Comm. Mkt. L.R. 413 (terms of the rulings of the Court of Justice provide guidance in determining whether or not the Treaty of Rome prevails over subsequent Belgian legislation). *See also* Van Gend en Loos v. Nederlandse Administratie der Belastingen, 1963 E. Comm. Ct. J. Rep. 1, 1963 Comm. Mkt. L.R. 105.

12. Treaty of Rome, *supra* note 1, art. 54(3)(g)

13. Treaty of Rome, *supra* note 1, art. 54(2). The independence of Commission members and their staffs from Member State influence is established in the Merger Treaty, *supra* note 1, art. 10(2). *See generally* STEIN, *supra* note 9, ch. 6.

14. Since June 1979, citizens of the member states have elected directly the 434 members of the Parliament. *See* 19 O.J. EUR. COMM. (No. L 278) 1 (1976).

15. Treaty of Rome, *supra* note 1, arts. 193–198. The Economic and Social Committee has advisory status, representing employees, workers, and various professional and consumer interests. The Committee's 156 members, appointed for four year terms, have jurisdiction over, inter alia, approximation of laws, *id.* art. 100, labor, *id.* art. 49, social issues, *id.* art. 63, and the right of establishment, *id.* art. 52.

16. *See, e.g.,* the Commisions revisions of its original texts of the proposed Seventh Directive on Company Law, *infra* notes 89-92.

The Council of Ministers conducts the final level of consideration, and normally operates in three stages. First, a "working party" of technical experts representing appropriate ministries of the Member States reviews the draft in detail, with a view to accommodating or eliminating the technical barriers to the Council's ultimate acceptance.[17] Second, the Committee of Permanent Representatives (COREPER) assesses the political acceptability of the proposed directive. COREPER, which includes representatives of ambassadorial rank from each of the Member States[18], may appoint staff panels to consider especially detailed or controversial proposals. Finally, the Council of Ministers itself, comprising the Foreign Ministers of the Member States,[19] has the power officially to issue directives having full legal effect. Because the Council generally takes action only if it has unanimous approval,[20] after the two earlier stages of review have produced an acceptable text, it rarely must expend much time over directives that do not in-

17. The Seventh Directive is the unusual instance where the working party could not eliminate the technical problems in a directive. *See infra* notes 107-111 and accompanying text.

18. In practice, the day-to-day work of COREPER is conducted at the level of the members' deputies. STEIN, *supra* note 9, at 228; *see* Merger Treaty, *supra* note 1, art. 4. The Merger Treaty speaks expressly of "permanent representatives." Merger Treaty, *supra* note 1, art. 4. Actual decision making, however, cannot be delegated to COREPER. The power of the final decision remains in the hands of the politically "responsible" Council of Ministers. *See* STEIN, *supra* note 9, at 227. With the exception of the Permanent Mission of Luxembourg, which consists of three persons, each Permanent Mission maintains a staff of 25 officials drawn mostly from the ministries of Foreign Affairs, but also including officials on detached service from ministries for Economic Affairs, Finance, and others. *Id.*

19. The Merger Treaty provides only that the Council include "members" of the Governments of the Member States. Merger Treaty, *supra* note 1, art. 2.

20. The Treaty of Rome would appear to authorize the adoption of company law harmonization directives on the basis of a qualified majority. *See* Treaty of Rome, *supra* note 1, art. 54(2). The qualified majority system is designed to require that a proposal obtain the assent of at least two of the four larger members (France, Germany, Italy, and the United Kingdom), but that those four must be joined by at least one smaller Member State for a proposal to be passed. *See* K. SIMMONDS, B2 ENCYCLOPEDIA OF EUR. COMMUNITY L. ¶ B10-337 (1973).

Since the adoption of the Luxembourg Compromise in 1966, however, the Council defers a vote in the absence of unanimity. The Luxembourg Compromise directs the Council to reach unanimous agreement on any issue as to which it is represented that "very important interests of one or more members are at stake." Extraordinary Session of the Council (January 1966): Second part of the session (28 and 29 January 1966), 3-1966 BULL. OF THE EUR. ECON. COMMUNITY 5, 8 (1966). Although the Luxembourg Compromise has no legal

volve the most important issues of Community policy.[21]

A directive may set a time limit within which implementing national legislation must be adopted. If a Member State does not observe such a time limit, or, in the absence of an express limit, if it does not enact legislation within a reasonable period of time, the Commission has the power to bring the offender before the European Court of Justice,[22] which can order the Member to comply forthwith.[23]

The Commission and the Council normally conduct their deliberations in private,[24] although they may and often do consult

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effect, the practice of the Council since 1966 has been to require unanimous approval of most significant decisions. *See* SIMMONDS, *supra.*

Recently the Luxembourg Compromise itself has again become an object of controversy. Angered over the refusal of the Council to revise its budget contribution, the United Kingdom attempted to veto the annual farm price review in the spring of 1982. Invocation of the Compromise was ruled out of order, and the vote on the price review proceeded to adopt the Commision proposals on a qualified majority basis.

The Treaty explicitly requires unanimous adoption of amendments to a Commission proposal. Treaty of Rome, *supra* note 1, art. 149. Similarly, decisions affecting the basic structure of the Community, such as admission of new members, require unanimous approval. *See* SIMMONDS, *supra* note 20, at ¶ B10-336.

21. Some problems have resulted, however, from adherence to the unanimity rule. Without the discipline which a majority rule imposes upon discussion, the legislative process suffers serious blockage at times. Marathon sessions have become a characteristic method of resolving difficult issues, particularly in the area of agriculture. Insofar as the unanimity rule impedes the "achievement of the Community's tasks," some critics assert that the rule violates article 5 of the Rome Treaty. *See* SIMMONDS, *supra* note 20, ¶ B10-337.

22. Treaty of Rome, *supra* note 1, art. 169.

23. Treaty of Rome, *supra* note 1, art. 171. *See, e.g.*, Comm'n of the Eur. Communities v. Italian Republic, 1980 E. Comm. Ct. J. Rep. 3635 (Italy's failure to implement, within the prescribed time period, Council Directive No. 73/361 on the approximation of the laws, regulations and administrative provisions of the Member States relating to the certification and marking of wire-ropes, chains and hooks, constituted a failure to comply with an obligation incumbent upon it under the Treaty); Comm'n of the Eur. Communities v. Kingdom of Belgium, 1980 E. Comm. Ct. J. Rep. 1473 (Belgium's failure to implement, within the prescribed time periods, a series of directives on the approximation of laws relating to the type-approval of motor vehicles and of agricultural tractors, constituted a failure to fulfill its obligations under the Treaty).

The Treaty is silent, however, on steps that may be taken should the Member State fail to comply with the judgment of the European Court of Justice.

24. The Commission's Rules of Procedure require that meetings of the Commission be closed to the public, and that all discussions be confidential. R. P. COMM'N, ch. 1, art. 8, 6-17 J.O. COMM. EUR. 181/63 (1963), 1974 O.J. EUR. COMM. 11 (special ed., 2d series).

affected industry or labor groups.[25] Parliamentary and ECOSOC debates are public, and Parliament often holds committee hearings with public witnesses on proposals under consideration.[26] Those parts of the legislative process that are open to the participation of the private sector do not discriminate against comments or suggestions from outside the European Community. It is therefore extremely important for U.S. and all non-EC businesses to understand the EC system, as well as its results which promise or threaten to regulate their operations. Because a well-reasoned supporting or opposing viewpoint is generally welcomed, participation by U.S. businesses in the EC legislative process in no way threatens, challenges, or denigrates the power of the Community to make laws; indeed, such participation manifests a sincere respect for the maturity of the developing EC sovereignty.

THE COMPANY LAW HARMONIZATION PROGRAM

The program to harmonize the company laws of the EC Member States encompasses ten directives.[27] Five directives have been issued by the Council, three have been proposed by the Commission and are in the legislative "pipeline," and two have not yet been submitted. In addition to these, two other legislative initiatives that would significantly affect the operations of companies in the European Community, are under consideration: the Vredeling Pro-

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25. For example, the Commission has circulated draft texts of the proposed Ninth Directive on company law within the EC in order to elicit business and labor reactions. *See infra* note 117 and accompanying text. Member State representatives on Council working parties frequently seek advice from their national chambers of commerce and from consumer or labor organizations.

26. Rule 89 of the European Parliament's Rules of Procedure requires the publication of the minutes of parliamentary proceedings in the *Official Journal of the European Communities*. Under Rule 104(2), committee meetings are not public unless the committee decides otherwise.

In the past, Parliament's committees have traditionally met in private. Since direct election of the Parliament in June of 1979, however, the public has been admitted to some committee meetings. A number of committees have organized public hearings to obtain the testimony of expert witnesses, or have routinely opened their doors to the public. *See* M. PALMER, THE EUROPEAN PARLIAMENT 87 (1981).

27. *See* Ficker, *The EEC Directives on Company Law Harmonization,* in HARMONIZATION OF EUROPEAN COMPANY LAW 66 (C. Schmitthoff ed. 1973) (descriptive analysis of the various company law directives proposed as of 1973).

posal on the dissemination of information to and consultation with workers' representatives, and a model charter of an EC corporation, the Societas Europea.[28]

The Directives Already Promulgated

The First Company Law Directive was issued in 1968.[29] Although significant controversy greeted its issuance as the Member States explored the new territory of company law harmonization,[30] the First Directive is substantively neither radical nor onerous. It has been implemented in all of the Member States.[31]

The First Directive covers three distinct issues: public disclosure, the validity of corporate acts, and the "nullity" of companies. It

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28. The basic policy of the EC regarding company laws and multinational enterprise was enunciated in a 1973 Commission report. *Multinational Undertakings and Community Regulations,* BULL. OF THE EUR. COMMUNITIES, SUPP. 15/73 (1973) (communication from the Commission to the Council) [hereinafter cited as Green Paper].

On the subject of EC harmonization generally, see STEIN, *supra* note 9; THE HARMONIZATION OF EUROPEAN COMPANY LAW (C. Schmitthoff ed. 1973); Berger, *Harmonization of Company Law under the Common Market Treaty,* 4 CREIGHTON L. REV. 205 (1971); Schmitthoff, *The Success of the Harmonisation of European Company Law,* 1 EUR. L. REV. 100 (1976); Silkenat, *Efforts Toward Harmonization of Business Laws Within the European Economic Community,* 12 INT'L LAW. 835 (1978); Stein, *Assimilation of National Laws as a Function of European Integration,* 58 AM. J. INT'L L. 1 (1964).

29. First Council Directive of 9 March 1968 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community, 1968(I) O.J. EUR. COMM. (No. L 65) 41 (special ed.) [hereinafter cited as First Directive].

30. *See generally* STEIN, *supra* note 9, ch. 6 (discussion of events leading up to promulgation of the First Directive).

31. Telex from the office of the European Commission in Brussels, Belgium to the Delegation of the European Communities in Washington, D.C. (Apr. 30, 1982) [hereinafter cited as Brussels Telex]. *See* implementing legislation of Belgium, Law of Mar. 6, 1973, MB (June 23, 1973); Denmark, Law No. 503, HM J No. 119 (Nov. 29, 1972); France, Ordonnance No. 69/1176, 1969 Journal Officiel de la Republique Francaise (Dec. 20, 1969); German Federal Republic, Law of Aug. 15, 1969, Bundesgesetzblatt, Teil 1 [BGB1] at 1146 (Aug. 18, 1969); Ireland, Statin No. 163 (June 20, 1973); Italy, Decree No. 1127, Gazetta Ufficiale della Repubblica Italiana No. 35 (Dec. 29, 1969); Luxembourg, Law of Nov. 23, 1972, Memorial A No. 72 1586 A 1594; Netherlands, Law of Apr. 29, 1971, Staatsblad voor het Koninkrijk der Nederlanden [Stb.] No. 285, law of May 28,

requires that companies[32] publish their articles of incorporation or charters and all subsequent amendments,[33] their balance sheets and profit-and-loss statements,[34] and various juridical acts which could affect creditors or shareholders.[35] Member States are ordered to record this information in central registers.[36] Although the First Directive expressly requires that these matters be published, it lacks specific detail concerning the form of the publication. The Fourth Directive addresses this issue.[37]

The First Directive protects third parties relying on apparent corporate acts against a defense of ultra vires, by preventing a de facto corporation from declining to assume obligations arising from its acts, and by assigning responsibility and legal liability to the individuals who performed them.[38] When a company purports to act in excess of its charter, an innocent third party may still hold the company liable for its actions.[39]

Finally, the First Directive provides that companies may be

1975, Stb. No. 227; United Kingdom, European Commmunities Act 1972.

32. The First Directive specifies the types of company organizations in each Member State to which the Directive applies and includes most of the common forms: the French, Belgian, and Luxembourgeois societe anonyme (S.A), the German Aktiengesellschaft (A.G.) and Gesellschaft mit beschraenkter Haftung (G.m.b.H.), the Italian societa per azioni (S.p.A.), and the Dutch and Belgian naamloze vennootschap (N.V.). First Directive, *supra* note 29, art. 1. It also includes forms akin to the U.S. limited partnership. Upon accession of the United Kingdom and Ireland, most companies of limited liability in those countries were also included. For country-by-country discussions of the various forms of business organizations in the EC, see DOING BUSINESS IN EUROPE, COMMON MKT. REP. (CCH).

33. First Directive, *supra* note 29, art. 2, para. 1(a)-(c).

34. *Id.* art. 2, para. 1(f).

35. Such acts include transfer of corporate headquarters, dissolution, certain judicial decisions, and details concerning liquidation. *Id.* art. 2, para. 1(g)-(k).

36. All documents and particulars subject to the disclosure requirements of the Directive must be kept in a file in a central register, commercial register, or companies register. *Id.* art. 3. Such information must also be published in the national gazette. *Id.* art. 3, para. 4. Copies of the documents may be obtained at cost by written application. *Id.* art. 3, para. 3.

37. *See infra* notes 56-68 and accompanying text.

38. The First Directive mandates the imposition of joint and several liability upon persons who act in the name of a company before the company has acquired legal personality, unless otherwise agreed. First Directive, *supra* note 29, art. 7.

39. The First Directive states that acts by the company shall be binding upon it "even if those acts are not within the objects of the company, unless such acts exceed the powers that the law confers or allows to be conferred on those organs." *Id.* art. 9, para. 1. The Directive, however, allows Member States to hold such acts not binding upon the company where the third party knew or should have known of their ultra vires character. *Id.*

declared "null," that is, void or voidable, in certain limited circumstances. Declarations of nullity are permitted only upon judicial decree entered for failure of legal capacity or prescribed formalities, or for violation of law or contravention of public policy.[40] A declaration of nullity may be contested,[41] and does not affect the validity of the company's obligations.[42]

Promulgated in 1976, the Second Directive[43] deals with the formation, maintenance, increase, and decrease of capital in the form of shares of public stock companies, the payment of dividends, and the acquisition of assets. It effectively precludes the formation of small stock companies by setting certain minimum levels of capitalization as a prerequisite for incorporation or authorization to do business.[44]

Although the Second Directive contained a time element of two years for implementation,[45] after more than five years, only the

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40. *Id.* art. 11. The permissive grounds for nullity are specifically and exhaustively listed in article 11.

41. Where the law of the Member State allows a third party to challenge the decision of nullity, the directive requires that the third party do so within six months of public notice of the decision. *Id.* art. 12, para. 1.

42. The directive states that nullity "shall not of itself affect the validity of any commitments entered into by or with the company without prejudice to the consequences of the company's being wound up." *Id.* art. 12, para. 3.

43. Second Council Directive of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent. 20 O.J. EUR. COMM. (No. L 26) 1 (1977) [hereinafter cited as Second Directive].

44. The Second Directive sets a minimum capital requirement of 25,000 European units of account (EUA) for a company to be incorporated or to obtain authorization to commence business. *Id.* art. 6, para. 1. If the equivalent of the European unit of account in national currency is altered so that the value of the minimum capital in national currency remains less than 22,500 European units of account for a period of one year, the Commission will order the Member State to amend its legislation to comply with the 25,000 EUA standard within one year. *Id.* art. 6, para. 2. The Directive provides for the periodic review of the minimum level required, in light of economic and monetary trends in the Community. *Id.* art. 6, para. 3.

45. The Second Directive required implementation by the Member States within two years of its notification, *i.e.*, by December 13, 1978. *Id.* art. 43, para. 1. The Directive provided, however, longer time limits in certain specified cases, such as application of particuliar provisions to companies already in existence, and application to

United Kingdom and Germany have implemented it.[46] The apparent reluctance to adopt the appropriate legislation probably stems not from ideological rejection, but from the view that specific national laws were already in advance of the EC "reform."

Adopted in 1978, the Third Directive[47] regulates mergers, including those formed by acquisition and those formed by the creation of a new company.[48] It requires that certain draft terms of the merger[49] be published and be publicly available at least one month prior to the approval of the merger, requires management to report the effect of any merger on the workforce, and gives workers' representatives the right to address shareholders' meetings considering the merger.[50] The Third Directive attempts to protect the interests of shareholders by requiring an evaluation of the draft terms by independent experts.[51] The report of the experts must specifically include an evaluation of the fairness and reasonableness of the proposed share exchange ratio.[52]

The Third Directive required implementation before October 1981,[53] but no Member State has met the deadline.[54] The simple failure by a Member State to implement a directive on schedule does

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unregistered companies in the United Kingdom and Ireland. *Id.* art. 43, para. 2.

46. Brussels telex, *supra* note 31. The European Commission has initiated infringement proceedings in the European Court of Justice against the following Member States for their failure to implement the Second Company Law Directive: Belgium, Case No. 148/81; Denmark, Case No. 187/81; France, Case No. 150/81; Ireland, Case No. 151/81; Italy, Case No. 136/81; Luxembourg, Case No. 149/81. Brussels Telex, *supra* note 31.

47. Third Council Directive of 9 October 1978 based on article 54(3)(g) of the Treaty concerning mergers of public limited liability companies. 21 O.J. EUR. COMM. (No. L 295) 36 (1978) [hereinafter cited as Third Directive].

48. *Id.* art. 2.

49. *Id.* art. 5.

50. *Id.* art. 6. This is the first use of Article 54(3)g of the Treaty of Rome specifically to protect employees, although the language appears neither to contemplate nor to preclude such use. *See supra* note 8 and accompanying text.

51. *Id.* art. 10.

52. *Id.* art. 10, para. 2.

53. The Third Directive required implementation by the Member States within three years of its adoption. *Id.* art. 32, para. 1. It provided exceptions to this time limit, however, in certain specified cases, such as application to unregistered companies in the United Kingdom and Ireland, and application of particuliar provisions to certain holders of convertible debentures and convertible securities. *Id.* art. 32, paras. 2-4.

54. Brussels Telex, *supra* note 31.

not trigger penalties automatically. It does, however, give rise to the possibility that the Commission may bring an action to compel implementation in the European Court of Justice.[55]

The Fourth Directive[56] establishes the technical requirements for the publication of corporate data required to be published by the First Directive.[57] The Fourth Directive is by far the most technical and most controversial of the company law directives yet in effect. It is currently in the process of implementation by the Member States.[58]

The Fourth Directive guides accountants in presenting, auditing, and verifying balance sheets, annual reports, profit-and-loss accounts, and notes. The most significant aspects of the Fourth Directive are:

1) The Directive sets only minimum standards for the Member States; through implementing legislation a particular Member State may impose stricter accounting rules.[59]

2) The Directive relies upon the accounting concept of a "true and fair view"[60] of corporate financial status, although the precise meaning of this notion varies among the Member States.[61] The Directive does not attempt to legislate

55. *See supra* notes 22-23 and accompanying text.

56. Fourth Council Directive of 25 July 1978 based on article 54(3)(g) of the Treaty on the annual accounts of certain types of companies. 21 O.J. EUR. COMM. (No. L 222) 1 (1978) [hereinafter cited as Fourth Directive].

57. *See supra* notes 29-42 and accompanying text.

58. As of April 1982, the United Kingdom, Belgium, the Netherlands and Denmark had enacted implementing legislation.

59. "The Member States may authorize or require the disclosure in the annual accounts of other information as well as that which must be disclosed in accordance with the directive." Fourth Directive, *supra* note 56, art. 2, para. 6.

60. "The annual accounts shall give a true and fair view of the company's assets, liabilities, financial position and profit or loss." *Id.* art. 2, para. 3. Paragraphs 4 and 5 cover the circumstances in which compliance with other provisions of the directive is incompatible with or insufficient to meet the requirement of paragraph 3. Where the provisions are found not to be sufficient to give a true and fair view, additional information must be given. *Id.* art. 2, para. 4. Where a provision is incompatible with the presentation of a true and fair view, that provision must be departed from. *Id.* art. 2, para. 5. Departure from the provisions must be noted and explanations offered for both the reasons for the departure and its effects on assets, liabilities, financial position and profit or loss. *Id.* Thus, the true and fair view requirement has precedence over the other provisions of the Directive.

61. Tax laws in several Member States require that annual accounts reflect some balance

standard interpretation.

3) The Directive contains detailed instructions on layout, valuation methods, means of publication, and audits.[62] It will, however, have no significant tax implications since it recognizes the sharp variations among the systems of taxation of the Member States.[63]

4) The Directive permits derogation in the cases of "small" and "medium-sized" companies.[64]

5) The Directive does not apply to "dependent companies" of "groups" whose "dominant companies" are organized under the laws of a Member State, pending adoption of the proposed Seventh Directive.[65]

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sheet and profit-and-loss account items in accordance with specific requirements of their tax treatment rather than in accordance with generally accepted accounting principles. *See* M. CLAYTON, D. COMM & J. HINTON, HANDBOOK ON THE EEC FOURTH DIRECTIVE 4 (1979) [hereinafter cited as FOURTH DIRECTIVE HANDBOOK]. To mitigate any impairment of a true and fair view caused by use of different accounting systems, the Directive requires disclosure of the effects of using tax-based valuation rules on the accounts. *Id.; see also infra* note 63.

62. *See generally* Fourth Directive, *supra* note 56, arts. 3-51. Section 2 of the Directive, which includes articles 3-5, is entitled "General provision concerning the balance sheet and the profit and loss account;" section 3, articles 8-14, covers "Layout of the balance sheet;" section 4, articles 15-21, sets out "Special provisions relating to certain balance sheet items;" section 5, articles 22-27, covers "Layout of the profit and loss account;" section 6, articles 28-30, contains "Special provisions relating to certain items in the profit and loss account;" section 8, articles 43-45, comprises "Contents of the notes on account;" section 9, article 46, is entitled "Contents of the annual report;" section 10, articles 47-50, deals with "Publication;" and section 11, article 51, concerns "Auditing."

63. The Directive details reporting and disclosure requirements. As such it does not seek to change the tax law of any Member State, rather it attempts to have a true and fair view presented even where different tax accounting systems are used. *See id.* arts. 2, 9, 10, 23-26, 30, 33, para. 2(a), 43, para. 1(10).

64. "The Member States may permit companies which on their balance sheet dates do not exceed the limits of two of the three following criteria: (1) balance sheet total: 4 million EUA, (2) net turnover: 8 million EUA, [or] (3) average number of employees during the financial year: 250, to adopt [simplified layout requirements]." Fourth Directive, *supra* note 56, art. 27.

65. Article 57 provides that "[u]ntil the entry into force of a Council Directive on consolidated accounts . . . the Member States need not apply to the dependent companies of any group governed by their national laws of the provisions of this Directive concerning the content, auditing and publication of the annual accounts of such dependent companies [under certain conditions]." *Id.* art. 57, para. 1. Similarly, article 58 provides an exemption with

6) Except as noted in (5) above, and with certain other extremely limited exceptions, the Directive applies on a company-by-company basis.[66] Thus, if a non-EC multinational corporation has subsidiaries in the Community that satisfy the requisite size criteria, each subsidiary is independently responsible for complying with the Fourth Directive.

Although the Fourth Directive has engendered serious controversy and much public discussion, from a jurisdictional point of view it is unassailable. Fourth Directive obligations are imposed only upon European companies.[67] The Directive is neither discriminatory nor extraterritorial. Government control over the format of required financial disclosure is exercised in many countries, including, of course, the United States.[68]

The most recent company law directive to have been approved by the Council of Ministers is the Sixth Directive.[69] It attempts to

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respect to the auditing and publication of the profit-and-loss accounts of such dominant companies. *Id.* art. 58, para. 1.

The Seventh Directive would govern preparation of, inter alia, group accounts and group annual reports much as the Fourth Directive does for individual companies. Proposal for a Seventh Directive pursuant to Article 54(3)(g) of the EEC Treaty concerning group accounts (submitted to the Council by the Commission on 4 May 1976), 19 O.J. EUR. COMM. (No. C 121) 2 (1976) [hereinafter cited as Proposed Seventh Directive]. For further discussion of the Proposed Seventh Directive, see *infra* notes 83–111 and accompanying text.

66. The Directive sets out exactly what types of companies are covered by it in each of the Member States. *See* Fourth Directive, *supra* note 56, art. 1, para. 1.

67. The Fourth Directive expressly applies only to certain listed "types" of companies. All these "types" include only enterprises organized under the laws of one of the Member States. *Id.; see also* FOURTH DIRECTIVE HANDBOOK, *supra* note 61, at 3. For instance, companies covered in the United Kingdom are "public companies limited by shares or by guarantee [and] private companies limited by shares or by guarantee." By contrast, draft versions of the Seventh Directive would assign certain consolidation and disclosure obligations regarding the "dominant undertakings" of EC companies, whatever their form and whatever the system of law that governs their incorporation or operations. Proposed Seventh Directive, *supra* note 65, art. 6, para. 1(a).

68. *See, e.g.*, 17 C.F.R. § 210 (1981) (form and content requirements for financial statements required by U.S. securities laws).

69. Council Directive of 17 March 1980 coordinating the requirements for the drawing up, scrutiny, and distribution of the listing particulars to be published for the admission of securities to official stock exchange listing, 23 O.J. EUR. COMM. (No. 1 100) 1 (1980) [hereinafter cited as Sixth Directive].

create a standard format for the prospectus issued by a company on its first public offering of shares,[70] and it has caused hardly any controversy. The Sixth Directive requires implementation by the Member States by September 1982.[71]

The Directives in the Legislative Process

One of the most radical and far-reaching initiatives in the company law harmonization program, the Fifth Directive[72] was proposed by the Commission to the Council in 1972. According to the usual constitutional procedures, the Council promptly referred the Directive to the Parliament where it lay dormant for nearly a decade.

The Commission text of the proposed Fifth Directive would generalize to the entire European Community a structure of corporate governance now in use only in Germany and The Netherlands.[73] It would require that companies establish a two-tier board system in which a supervisory board would appoint and

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70. *Id.* Preamble paras. 7-9.

71. *Id.* art. 27, para. 1.

72. Proposal for a fifth directive to coordinate safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of article 58 of the Treaty, as regards the structure of societes anonymes and the powers and obligations of their organs, 15 O.J. EUR. COMM. (No. C 131) 49 (1972) [hereinafter cited as Fifth Directive]. For a discussion and analysis of the Fifth Directive, see Comm'n of the Eur. Communities, *Proposal for a Fifth Directive on The Structure of Societes Anonymes,* 32 BULL. E.C., 1 (Supp. 10 1972) (article by article analysis of the Fifth Directive); Conlon, *Industrial Democracy and EEC Company Law: A Review of the Draft Fifth Directive,* 24 INT'L & COMP. L. Q. 348 (1975) (describing influence of German company kawa); Lang, *The Fifth EEC Directive on the Harmonization of Company Law,* 12 Common Mkt. L.R. 155, 325 (1975) (discussing Fifth Directive in relation to British and Irish law).

In May 1982 Parliament completed its deliberations on the proposed Fifth Directive. The parliamentary text suggested that numerous amendments to the Commission version. Its thrust is to eliminate the mandatory character of the original proposal so that, for example, unitary boards will still be permissible in countries, such as Ireland and the United Kingdom, where they have been the tradition. The impact of Parliament's text on multinationals headquartered outside the EC is still unclear. 25 O.J. EUR.COMM. (No. C 149) 17(1982).

73. *See* Ottervanger & Pais, *Employee Participation in Corporate Decision Making,* 15 INT'L LAW. 393, 398 (1981). The Fifth Directive would apply only to certain types of companies in the Member States, *e.g.,* in Germany, the Aktiengesellschaft, in Belgium, France, and Luxembourg, the societe anonyme, in Italy, the societa per azioni, and in Belgium and The Netherlands, the naamloze vennootschap. Fifth Directive, *supra* note 72, art. 2, para. 1.

oversee a management board actually to run the company.[74] Under the Directive, enterprises with more than 500 employees would be required to reserve at least one-third of the seats on the supervisory board for representatives chosen by employees or their unions.[75]

The Fifth Directive raises a host of juridical problems. First, its requirements run counter to traditional corporate forms in English and U.S. law.[76] For example, the Directive's provision for corporate control by individuals who neither have an ownership interest, nor are answerable to the owners, is inconsistent with the power of shareholders ultimately to decide the course of the company.[77]

Supporters of the Fifth Directive do not shy away from charges of radicalism.[78] They assert that in today's complex and troubled economies, the "pure" form of corporate governance is an anachronism. Large companies have social responsibilities; they have become public actors in control of the lives of their employees, and often of their communities as well.[79] Thus, the modern age re-

74. Fifth Directive, *supra* note 72, art. 2, para. 1, art. 3, para. 1. Note that this analysis is based on the Commission's proposed text, and not that recommended by Parliament. The Commission is expected to respond formally to the latter in early 1983.

75. *Id* art. 4. An alternate approach under the Fifth Directive for companies with 500 or more employees is to allow the supervisory organ to appoint its own members subject to objection by the general meeting or representatives of the workers on the grounds that the appointee lacks the ability to carry out his duties or that a particular appointment would cause an imbalance in the composition of the supervisory organ with regards to the interests of the company, the shareholders or the workers. *Id.* art. 4, para. 3.

76. As long ago as Lord Coke, it was well established that a corporation was a company of persons "made into one body," and, at least in legal fiction, manifesting a single identity. The Case of Sutton's Hospital, 10 Co.Rep. 32b. U.S. law similarly views the corporate form not as a forum for exchange of social views but as a legal entity, existing for the purposes set out in its charter. *See* Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 636 (1819) .

77. *See, e.g.,* MODEL BUSINESS CORP. ACT §§ 28-34 (1971) (detailing the voting rights of stockholders of corporations governed by the Act).

78. *See, e.g., Report on Enterprises and Governments in International Economic Activity,* 1981-1982 EUR. PARL. DOC. (No. 1-169) (1981) [hereinafter cited as *Caborn Report*]. *See also* Green Paper, *supra* note 28:

> It should be pointed out that almost all the measures briefly analysed below are or will be carried out primarily in order to attain Community objectives which go beyond that of supervising the operations of multinational undertakings. This is particularly true of everything relating to the attainment of economic and monetary union or, for example, to taxation or social policy. That is to say that virtually all the measures the Community might take with regard to multinational undertakings relate to problems which may equally well be created by national undertakings or even by private individuals.

Id. at 7-8.

79. *See Caborn Report, supra* note 78: "Where there is a danger that multinationals may

quires more social control over corporations. The debate over corporate control is, of course, fundamental. Regardless of the specific content of the Fifth Directive, if any variant of it is enacted, this debate will continue within the EC. In a significant development, the European Parliament, in April 1981, adopted a report calling for increased control of multinationals, including mandatory information disclosure and more diligent enforcement of rules regulating competition and the protection of employees' interests.[80] The adoption of this report indicates that there is at least a good measure of support for the policy behind the Fifth Directive.

The commission draft of the Fifth Directive also contains provisions concerning the selection, independence, and payment of outside auditors.[81] As is apparent from consideration of the Seventh and Eighth Directives ,[82] EC institutions view the harmonization of audit practices as an essential component of the company law project.

The Commission first proposed the draft Seventh Directive to the Council in 1976.[83] After review by Parliament[84] and ECOSOC,[85] the Commission revised the proposal in late 1978.[86] By establishing procedures for the consolidation of accounts of "groups" of companies, the Seventh Directive would regulate dependent enterprises not covered by the Fourth Directive.[87] The drafters of the Seventh Directive maintain that only if consolidated reports are filed can an accurate picture of the role of related enterprises in the Community be derived.[88]

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damage the social market economy by abusing an oligopolistic position and exploiting differences in national legislation or disregarding the rules of bipartite consultations, it should be possible for the authorities to take the necessary corrective measures." *Id.* at 5.

80. The so-called Caborn Report was adopted by Parliament on April 15, 1981. *Caborn Report, supra* note 78. The Report was adopted nothwithstanding Parliament's right-of-center majority.

81. Fifth Directive, *supra* note 72, arts. 53-57.

82. *See infra* notes 83-116 and accompanying text.

83. Proposed Seventh Directive, *supra* note 65.

84. 21 O.J. EUR. COMM. (No. C 163) 60 (1978). Parliament suggested that the Seventh Directive be changed. In particular, it urged the adoption of the worldwide consolidation option for non-EC parents, and the deletion of obligations to publish subgroup consolidations when the dominant undertaking itself must publish a consolidated report. *Id.* at 61.

85. 20 O.J. EUR. COMM. (No. C 75) 5 (1977). ECOSOC, like Parliament, endorsed the draft "in principle" but proposed numerous technical and textual changes. *Id.* at 6-9.

86. 22 O.J. EUR. COMM. (No. C 14) 2 (1979) [hereinafter cited as Amended Proposed Seventh Directive].

87. *Id.* arts. 5, 6.

88. The preamble to the Amended Proposed Seventh Directive recites that "annual

The consolidation requirements of the Seventh Directive create an obvious problem for multinational corporations not headquartered in the EC. The consolidation of separate subsidiaries of foreign parents would be both difficult and misleading, if, for example, those subsidiaries were in different industrial sectors, were managed independently, and shared only their ultimate parentage and their location in EC Member States. Nevertheless, in its original versions, the draft made no special allowance for the compliance problems of foreign multinationals.[89] It simply required EC-wide consolidations to include all related enterprises located in or controlled from the Community.[90] As might be expected, non-EC chambers of commerce and employers' federations objected strenuously to this requirement, claiming that compliance would be extremely costly and of little value.[91]

As a result of these vehement protests, the working party of the Council proposed certain compromises. Member States would be permitted to allow non-EC enterprises to produce either European Community sub-consolidations or worldwide consolidations at their option. The working party, however, added one proviso: worldwide accounts would have to be "comparable" or "equivalent" to the consolidations required of EC companies by the Directive.[92]

Commission officials have repeatedly assured U.S. multinational corporations that Form 10-K, regularly filed with the U.S. Securities and Exchange Commission, would satisfy Seventh Directive obligations as set out in the amended text. Those assurances

accounts of companies belonging to a group cannot by themselves give a true and fair view of their position." *Id.*

89. *See* Proposed Seventh Directive, *supra* note 65.

90. *Id.* art. 6.

91. *See* American Chamber of Commerce in Belgium, Memorandum on the Amended Proposal for a Seventh Directive Pursuant to Article 54(3)(g) of the EEC Treaty Concerning Group Accounts, Sept. 13, 1979. The Chamber asserted that the requirement for Community consolidations will present an "unacceptable burden" to groups dominated by non-EC companies, and questioned the ultimate usefulness of the information required. *Id.* at 3. *See also* National Foreign Trade Council, Inc., Comments on Proposed Seventh Directive Pursuant to Article 54(3)(g) of the EEC Treaty Concerning Group Accounts, Apr. 14, 1980. The National Foreign Trade Council asserted that the proposed reporting requirement, insofar as it related to non-EC based multinationals, was deficient in two major respects: the envisaged consolidations would fail in certain circumstances to reflect economic reality; and developing the necessary information would present substantial technical accounting difficulties. *Id.* at 3-5.

92. Unpublished drafts of the EC Council Working Party (copy on file at the offices of *Law & Policy in International Business*).

should be viewed, however, as subject to two caveats. First, the Commission cannot guarantee that Member States in their implementing legislation will take as lenient a view of foreign filings as the Commission does.[93] Proponents of the Directive respond that Member States, inclined to impose onerous disclosure requirements on foreign companies doing business in their territory, do not need an enabling EC directive; they are free to adopt such legislation, whatever the law imposed at the Community level.[94] Second, the worldwide consolidation option is of little use to privately-held companies outside the Community which are not required to disclose worldwide accounts even in their countries of incorporation.[95] This consideration has evidently left Commission officials unmoved, perhaps because of the very small number of foreign closely-held corporations operating in Europe, as well as because of the not uncommon but erroneous mistrust of the privately-held company.

Compliance difficulties encountered by closely-held companies exemplify an even more fundamental challenge posed by the various drafts of the proposed Seventh Directive. A subsidiary corporation has no legal right to demand access to information held by its parent.[96] Although in practice the kinds of information to be provided by foreign companies under the Seventh Directive—for example, worldwide accounts—are commonly available to European subsidiaries, such disclosure is not required as a matter of law.

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93. Member State implementing legislation would actually impose legal obligations upon individual companies. A directive is addressed to Member States. *See supra* notes 10-12 and accompanying text; Proposed Seventh Directive, *supra* note 65, art. 27. Under the Treaty of Rome, the Member States would be free to select the "forms and methods" of achieving the directive's "result." Treaty of Rome, *supra* note 1, art. 189. It is unlikely that the European Court would hold Member State legislation which required information substantially different from that included in a Form 10-K to be an abuse of that freedom.

94. If it is within the sovereign authority of a Member State to enact legislation in response to a Community directive, it must be within that State's authority to enact such legislation on its own initiative. The Treaty of Rome does not expand the Member States' legal powers to regulate trade or business within their own borders, or with respect to their own citizens.

95. SEC filing requirements, for example, are not generally applicable to privately-held companies but are triggered by the number of a company's shareholders. *See* 15 U.S.C. § 78 l(g) (1976).

96. *See* H. HENN, HANDBOOK OF THE LAW OF CORPORATIONS (1961). A parent corporation and its subsidiary are generally treated as separate and distinct entities, even if the parent owns all the shares in the subsidiary and the two enterprises share directors and officers. *Id.*

A publicly-held company is unlikely to object to an EC requirement that a few more copies of its annual report or its Form 10-K be printed. In contrast, the obligation imposed upon subsidiaries to present worldwide information concerning their parent could be viewed as an example, albeit perhaps a minor one, of extraterritoriality that is impermissible under principles of international law. While a nation may not, in general, mandate or proscribe activities by aliens outside of its borders, most states recognize an exception to this rule when foreign conduct causes direct domestic effects.[97] Both the United States[98] and the EC[99] recognize such a rule, along with its limited exceptions.[100] Even the doctrine of direct effects, however, does not provide a basis for ongoing extraterritorial regulation of foreign business operations.

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at 206-07.

97. See the discussion of the territorial and nationality principles in Jacobs, *Extraterritorial Application of Competition Laws: An English View,* 13 INT'L LAW. 645, 647 (1979). It is arguable that the Seventh Directive contravenes these principles since the information sought is located outside the EC and no one in the community has a legal *right* of access to it. *See* National Foreign Trade Council, Inc., Comments on Proposed Seventh Directive Pursuant to Article 54(3)(g) of the EEC Treaty Concerning Group Accounts, Apr. 14, 1980 (copy on file at the offices of *Law & Policy in International Business).* Those who allege that the Directive operates extraterritorially assert that any "direct effects" in Europe caused by multinational companies are produced through EC subsidiaries which are themselves already subject to the Fourth Directive.

98. Judge Learned Hand formulated the "direct effects" doctrine in U.S. law: "It is settled law . . . that any state may impose liabilities, even upon persons not within its allegiance, for conduct outside its borders which the state reprehends." United States v. Aluminum Co. of Am. 148 F.2d 416, 443 (2d Cir. 1945). Some U.S. courts first balance matters of comity before examining the directness of effects on the United States. *E.g.,* Mannington Mills v. Congoleum Corp., 595 F.2d 1287, 1297-98 (3d Cir. 1979). *See generally,* H. STEINER & D. VAGTS, TRANSNATIONAL LEGAL PROBLEMS 932-1085 (2d ed. 1976); Garvey, *The Foreign Trade Antitrust Improvements Act of 1981,* 14 LAW & POL'Y INT'L BUS. 1 (1982); Jacobs, *supra* note 97, at 649-53; Note, *Antitrust Law: Extraterritoriality* 20 HARV. INT'L L.J. 667, 670 (1979).

99. *See generally* STEINER & VAGTS *supra* note 98, at 1394-1405, 1417-19; Imperial Chemical Industries Ltd. v. Commission of the European Communities, 1972 E. Comm. Ct. J. Rep. 619, 11 Common. Mkt. L.R. 557 (EC formulation of the "direct effects" doctrine is applied.)

100. *See* Garvey, *supra* note 98, at 6-19; Jacobs, *supra* note 97, at 650-52; Note, *supra* note 98, at 667. *See also,* Mannington Mills v. Congoleum Corp., where the court used a balanc-

In response to the charge that the Seventh Directive would apply extraterritorially, EC officials argue that worldwide consolidation is simply an option offered for the convenience of foreign companies, and that non-EC companies may, if they choose, produce only EC accounts.[101] They assert that because the operations of foreign parents directly affect the European economy, any extraterritorial reach is justified,[102] and that it is inappropriate for businesses in the United States, the extraterritoriality of whose laws in the area of competiton has long been criticized, to raise this objection.[103] Nevertheless, the proposed Seventh Directive does differ from the directives already enacted, whose obligations affect only companies incorporated in the Member States. Some commentators, therefore, see the Seventh Directive as evincing an underlying fundamental distrust of multinational corporations, which expresses itself by requiring full disclosure as the price of doing business in Europe.[104]

Whether that distrust would in fact be reduced by the Seventh Directive is unclear. The many weaknesses in the language of the various drafts have created uncertainty about its actual meaning and potential impact. Numerous key terms—"group," "consolidated account," and "EC subgroup,"—are left undefined, or are

ing test of ten factors to determine whether "direct effects" jurisdiction should have been exercised. 595 F.2d at 1297-98.

101. Amended Proposed Seventh Directive *supra* note 86, art. 7a, para. 4.

102. *See* The Seventh Directive on Consolidated Accounts: The Present Position 6 (Apr. 1980) (EEC paper summarizing directive) (copy on file at the offices of *Law & Policy in International Business*).

103. Karl Gleichman, head of the EEC Commission's multinationals department said that it was "curious to see Americans complaining about the extraterritoriality of laws. Often, it is precisely this aspect of U.S. antitrust rules which other countries complain about." Int'l Herald Tribune, Oct. 27, 1981, at 11, col. 1.

The United Kingdom and France have recently enacted legislation to combat the allegedly impermissible extraterritorial effect of U.S. antitrust laws. *See* Herzog, *The 1980 French Law on Documents and Information,* 75 AM. J. INT'L L. 382 (1981); Love, *Blocking Extraterritorial Jurisdiction: The British Protection of Trading Interests Act, 1980,* 75 AM. J. INT'L. L. 257 (1981); Pettit & Styles, *The International Response to the Extraterritorial Application of U.S. Antitrust Laws,* 37 BUS. LAW. 697 (1982).

104. Senator Symms apparently perceived such distrust when he introduced "a bill to provide protection from requirements and prohibitions imposed upon citizens of the U.S. by foreign nations concerning the disclosure of confidential business information and for other purposes." S. 1592, 97th Cong., 1st Sess. 1, 127 CONG. REC. S9230 (daily ed. Aug. 3, 1981). The Senator said that "the European institutions are trying to compel U.S. companies to make public and ultimately to subject to European control their every move—worse, their every contemplated move." 127 CONG. REC. S9230 (daily ed. Aug 3, 1981) (remarks of Sen. Symms).

defined only in unhelpful ways.[105] As it has been drafted, the Directive would require that the "equivalence" of foreign filings be certified by auditors in each Member State, thus creating the potential for different consolidations to be required in different countries.[106] Nor does the Directive contain specific instructions concerning currency valuation or language, and this too could lead to anomalous and onerous results for companies.

The accounting and technical problems in the text of the Directive have led to an unusual development in the legislative process. The working party of the Council terminated its work in December 1981 without having agreed upon a single, definitive text to refer to COREPER. Instead, it proposed alternative solutions to several important questions, including: whether "actual control" of one company by another, absent unified management or substantial shareholding, creates a "group" relationship;[107] whether small groups should be exempted, and if so, how such an exemption should operate;[108] whether parent companies that are not limited liability companies should be included;[109] and whether to require or permit the inclusion of single EC companies actually managed as groups together with companies outside the EC.[110]

The inability of the working party to reach agreement has posed extremely technical problems for COREPER. COREPER has, therefore, had to appoint its own working group in order to resolve these matters, and the transmittal of a final text to the Council will thus be delayed. At present, few observers believe that the Seventh

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105. *See* Amended Proposed Seventh Directive, *supra* note 86, arts. 6–8.

106. The unpublished final draft of the EC Council Working Party, art. 7a, para. 4(a) (Aug. 1981) substituted the word "equivalent" for the word "comparable" used in the Amended Proposed Seventh Directive, *supra* note 86, art. 7a, para. 4(a). [hereinafter cited as Working Party Seventh Directive] (copy on file at the offices of *Law & Policy in International Business).*

The difference in required consolidations among the member states is possible because each member nation's implementing legislation, and not the directive, imposes legal obligations. Member States are required only to legislate for the "result to be achieved" under the directive, and may select the "form and methods" themselves. *See* Treaty of Rome, *supra* note 1, art. 189; *See also supra* note 1 and accompanying text.

107. The alternative formulations are contained in Working Party Seventh Directive, *supra* note 106, art. 6, para. 1(d).

108. *Id.* art. 6, para. 6.

109. *Id.*

110. *Id.* art. 7, para. 1.

Directive will be issued before the middle of 1983, even if the questions that are still outstanding are resolved rapidly by compromises rather than by extensive rewriting.[111]

First submitted by the Commission to the Council in April 1978, the Eighth Directive has since been revised, and the current text was published in December 1979.[112] The proposal, which concerns the professional qualifications of auditors,would not create a general cross-border right to practice,[113] but it does set out conditions under which auditors qualified in one Member State would be able to conduct audits in another.[114] This capability would be especially important upon adoption of the Seventh Directive, because it would avoid the unnecessary, potentially confusing, and extremely costly duplication of audit reports. An auditor certified under the Eighth Directive could issue a single opinion for a group or subgroup consolidation that would be accepted by all Member States requiring such a report. For example, once an auditor has certified accounts as satisfying the requirements of the Seventh Directive, separate certification should not be necessary in the other Member States.

The draft Eighth Directive also would require Member States to maintain official registers of qualified auditors, would provide for the independence of auditors, and would specify the forms of business association available to them.[115] These provisions have en-

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111. Recent unofficial reports indicate that the COREPER working group may decide to delete article 7a, which would have affected EC subsidiaries of foreign parents. The committee is said to have removed the obligation of publishing "artificial horizontal subgroup consolidations" by companies which are not actually managed by—or in conjunction with—other enterprises in the EC. If independent subsidiaries of non-EC parents are exempted, the option of producing parents' worldwide accounts falls as well, since it was offered as a facility for complying with the EC consolidation requirement.

If these reports are correct, the most likely result would appear to be that subsidiaries of foreign parents must annotate their Fourth Directive accounts to reflect intra-corporate transactions, including the sharing of overhead and expenses. Exactly what would be included in such annotations is still extremely unclear.

112. Amended Proposal for an Eighth Directive founded on Article 54(3)(g) of the EEC Treaty concerning the approval of persons responsible for carrying out statutory audits of the annual accounts of certain types of company, 25 O.J. EUR. COMM. (No. C 317) 6 (1979) [hereinafter cited as Eighth Directive].

113. The Eighth Directive does not go as far as "the effective exercise by lawyers of freedom to provide services," which permits lawyers to practice anywhere in the EC. Council Directive of Mar. 22, 1977, 20 O.J. EUR. COMM. (No. L 78) 17, art. 1 (1977).

114. Eighth Directive, *supra* note 112, art. 4.

115. *Id.* arts. 11, 12.

gendered considerable controversy within the accounting profession, and could be responsible for the delay in the Directive's adoption, which originally had been expected in late 1981[116]

The Directives Not Yet Formally Proposed

Of all the legislative proposals included in the company law harmonization program, the draft Ninth Directive, which concerns the organization of groups of companies, is, by general consensus, the most radical. Although no final text has yet been submitted by the Commission to the Council, the Commission's working draft, together with a lengthy analytical commentary, has been widely circulated in Europe since January 1981.[117]

The Ninth Directive would attempt to encourage parent companies to conclude "control contracts" with their subsidiaries. A control contract — a creature known only to German law and not widely seen even in the Federal Republic[118] — is an agreement whereby the parent guarantees certain obligations of the subsidiary vis-a-vis third parties, such as employees, creditors, and minority shareholders. Control contracts are designed to protect third parties against default by a subsidiary, by requiring the parent to issue certain guarantees in exchange for the right of management. Minimum capitalization requirements for the dependent company are normally waived, because an injured third party would have recourse to the parent's assets.[119]

The debate over the Ninth Directive has so far been characterized by the absence of public statements of strong support for the initiative. Unlike other parts of the company law harmonization program, it has received little support even from the trade unions.[120]

116. Synopsis, Apr., 1981, at 2 (newsletter issued by the Continental Office of Ernst & Whinney).

117. Proposal for a Ninth Directive Based on Article 54(3)(g) of the EEC Treaty on Links Between Undertakings, and in Particular on Groups [hereinafter cited as Ninth Directive] (copy on file at the offices of *Law & Policy in International Business*).

118. For an analysis of the German Aktien Gesetz of 1965, see Matomura, *Protecting Outside Shareholders in a Corporate Subsidiary: A Comparative Look at the Private and Judicial Roles in the United States and Germany,* 1980 WIS. L. REV. 61, 68–71. The German law applies only to the Aktien Gesellschaft (A.G.) in Germany. The draft Ninth Directive is much wider and covers, for example, French and Belgian societes anonymes. Ninth Directive, *supra* note 117, art. 1, para. 1. Both the limited coverage of the German law and the broad scope of the Directive argue against rapid expansion without reasonable cause. That is, total EC experience with control contracts is limited to a comparatively few companies in one single Member State.

119. *See generally* Matomura, *supra* note 118.

120. The European Trade Union Congress (ETUC) testified passionately and effectively

Because parent companies have not, in the past, manifested any pattern of willingness to tolerate defaults by their subsidiaries, it is not likely that control contracts would reduce the frequency or mitigate the effects of such defaults.

Opponents of the Ninth Directive have objected vehemently to many of its provisions.[121] The greatest amount of criticism has been directed at the means it uses to coax companies toward the control contract model. Since the purpose of control contracts is to provide a form of guarantee by the parent company of certain of its subsidiary's obligations, the Commission draft legislates a comparable guarantee where the control contract has not been used.[122] The draft provides that when management undertakes actions that inure to the detriment of the subsidiary, not only is the parent company liable to those who may be injured, but the members of the parent's board must bear joint and several unlimited liability.[123] That a decision affecting the subsidiary may substantially benefit other companies in the same group is not a defense.[124] Nor is directors' liability in any way conditioned upon their failure to meet any recognized standard of prudence or of business judgment.[125] Thus, under the Ninth Directive, foreign multinationals would confront an impossible dilemma: either to elect the unfamiliar and cumbersome control contract, or to submit their directors to potential personal liability. Neither option is palatable; nor, on the available evidence, is the need to make such a choice in any way justified.

Other Ninth Directive requirements are equally extraordinary. The draft requires public notice whenever blocks of shares in companies are acquired by other enterprises,[126] and periodic reports

at the Parliamentary Social Affairs Committee hearings in October, 1981, in support of the Vredeling Proposal. *See infra* notes 143-179 and accompanying text; *Caborn Report, supra* note 78. The Caborn Report is an eloquent defense of the spirit of the Vredeling Proposal as well as of the Fifth Directive. There has been no similar show of union support for the proposed Ninth Directive.

121. *See* Council of American Chambers of Commerce – European and Mediterranean, Memorandum on the Proposed Ninth Directive on Company Law (Sept. 1981) [hereinafter cited as Chambers Comments] (copy on file at the offices of *Law & Policy in International Business)*; National Foreign Trade Council, Memorandum Concerning the Proposed Ninth EC Directive on Company Law (Nov. 20, 1981)[hereinafter cited as NFTC Comments] (copy on file at the offices of *Law & Policy in International Business).*

122. See Ninth Directive, *supra* note 117, Commentary at 64, and arts. 7-12.

123. *Id.* art. 7.

124. *Id.* art. 8(1)(c).

125. *Id.* art. 7(2)(a). A member may, however, be relieved of liability if he can prove that the influence giving rise to the damage is not attributable to him. *Id.* art. 7(2)(b).

126. The obligation to report is triggered by the acquisition of shares representing 10, 25,

detailing all activities undertaken by a subsidiary for the benefit of its parent, including actions which have failed to benefit the subsidiary.[127] A shareholder, creditor, or employees' representative may protest any notice or report, and may call for an independent audit to be conducted at the company's expense.[128] Should the auditor—who has subpoena authority—uncover allegations that the subsidiary has been "influenced" and thereby "damaged," the courts would have authority to prevent or mitigate the damage by a variety of means, including suspending directors or issuing injunctions against further "damaging measures."[129] The only way for a company to avoid these results would be to institute a control contract form of organization.[130]

The Directive purports to guarantee the position of minority shareholders, by assuring them of the right to be bought out, either in cash or through annual "equalization payments," based upon estimated future earnings.[131] All calculations of proper values to be offered may be challenged in litigation,which may result in an injunction against the proposed valuation or transaction, and/or the removal of the board members.[132]

The Ninth Directive is aimed, as some would argue the entire harmonization project is aimed,[133] at the decentralization of corporate management. Its language is facially inconsistent with the obligation of a board of directors to defend the interests of its company or group of companies, an obligation upheld by the French courts, for example, in *Fruehauf Corporation v. Massardy*.[134] In

50, 75 and 90 percent of a company. Ninth Directive, *supra* note 117, art. 6, para. 1. Whenever a shareholder owning more than 10 percent of a company increases or decreases his holding by more than 5 percent, he must notify the company in writing and, until that notice is given, the shareholder may not exercise rights attaching to his shares. *Id.* art. 5, para. 1.

127. *Id.* art. 8.

128. *Id.* art. 9.

129. The Directive provides that a court or authority competent under national law may, if it is necessary to protect the company, its shareholders, or employees: a) suspend management from office; b) enjoin performance of a "damaging" contract; and c) require the parent corporation to buy out the subsidiary's shareholders. *Id.* art. 10, para. 1.

130. *See id.* art. 12.

131. "Independent experts" appointed by the management will give their opinion on the appropriateness of the offers made for the stock and the method of valuation. *Id.* arts. 10, para. 1(c), 15-17.

132. *Id.* art. 10.

133. *See* Green Paper, *supra* note 28.

134. [1968] D.S. Jur. 147 (Cour d'appel, Paris, 1965). *See* 5 INT'L LEGAL MATERIALS 476 (1966). For an analysis of the case, see W. L. Craig, *Applications of the Trading with the Enemy*

Fruehauf, the *Cour d'appel* of Paris sharply delineated the overriding responsibility of directors to their company in ordering a French subsidiary of a U.S. company to perform a contract allegedly barred under U.S. law. The Court responded to "the interests of the company rather than the personal interests of any shareholders even if they be the majority."[135] Indeed, the *Fruehauf* case, which concerned the application of the U.S. Trading with the Enemy Act of 1917, demonstrates that directors' obligations can differ even from the interests of the shareholders. Directors are obligated to act in a fiduciary capacity with respect to their company. As long as they act prudently and faithfully, they are protected from personal liability. Prudent and faithful directors may determine, and in some cases may even be required to determine, that one part of their company must be harmed in order to benefit the whole. Directors must be free to pursue the interests of the company, or group of companies, with whom they have assumed a fiduciary relationship.

The Ninth Directive was to be submitted by the Commission to the Council in the autumn of 1981. Because it has met a firestorm of opposition, mostly from European sources, the Directive has been so delayed that it has not yet been finalized. Rumors abound that the project has been returned to the Commission staff for substantive revision. The Ninth Directive is likely to be amended substantially before publication to make it less radical. It is of course possible that it will never be submitted, or that, after being issued by the Commission, it will be left in suspended animation as was the Fifth Directive.[136] Nevertheless, that such a proposal has even been put forward is significant. EC institutions have demonstrated a willingness to propose fundamental changes in the operation of companies outside the Community, if they perceive such changes as somehow beneficial to companies within their jurisdiction. They are not seriously deterred by the doctrine of extraterritoriality,[137] or by the charge that their proposed initiatives are impermissible according to principles of international law and comity.

An intelligent reaction to a proposal such as the Ninth Directive must include an acknowledgement that the EC is, at present,

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Act to Foreign Corporations Owned by Americans, 83 HARV. L. REV. 579 (1970).

135. "[L]e juge des référés doit s'inspirer des intérêts sociaux par préférence aux intérêts personnels de certains associés, fussent-ils majoritaires." [1968] D.S. Jur. at 148.

136. *See supra* note 72.

137. *See supra* note 97 and accompanying text.

confronting an extraordinarily harsh economic and political climate. Unemployment has reached levels undreamed of since World War II and is continuing to climb.[138] The voters of France and Greece have elected socialists as national leaders,[139] and since January 1981, the governments of Ireland, Denmark, The Netherlands, Germany, Italy, and Belgium have fallen.[140] The United Kingdom has once again vehemently protested what it sees as its excessive contribution to the Community in the annual budget review.[141] In short, there are fundamental problems in maintaining the political and economic unity that has been attained by the European Community. It is not surprising, then, that EC officials may assign to the survival of the Community an importance greater than that given to traditional, and arguably outdated, precepts of corporate law.[142]

OTHER MEASURES RELATED TO COMPANY LAW HARMONIZATION

The Vredeling Proposal

More than any other EC initiative, the so-called Vredeling Proposal[143] has been responsible for the sudden increase in awareness in the United States of developments in European law. The Proposal is named for its originator, the Dutch Socialist Henk Vredeling, whose term as Commissioner for Employment and Social Affairs ended on December 31, 1980.[144] If adopted, the Vredeling Proposal would

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138. Official statistics show 10.7 million unemployed workers in the European Community in February 1982, 9.7 percent of the civilian work force. Statistical Office of the European Communities, *Unemployment,* MONTHLY BULL., Feb. 1982.

139. Francois Mitterand, was elected President of France on May 10, 1981. N.Y. Times, May 11, 1981, at A1, col. 3. Andreas Papandreou became Prime Minister of Greece on October 18, 1981. *Id.*, Oct. 20, 1981, at A11, col. 3.

140. Belgium, Denmark, and Ireland have each had three governments since January 1981. *Id.*, Dec. 8, 1981, at A5, col. 3; *id.*, Dec. 23, 1981, at A4, col. 1; *id.*, Jan. 28, 1982, at A3, col. 1. Giovanni Spadolini became Prime Minister of Italy on June 28, 1981. *Id.*, June 29, 1981, at A1, col. 5.

141. *Id.*, May 30, 1981, at A7, col. 1.

142. The Tenth Directive would govern the dissolution or winding-up of companies. As of the beginning of 1982, there was no information available about the Tenth Directive, which is apparently still in the early drafting stages within the headquarters of the EC Commission. *See* Synopsis, *supra* note 116, at 2.

143. Proposal for a Council Directive on procedures for informing and consulting the employees of undertakings with complex structures, in particular transnational undertakings, 23 O.J. EUR. COMM. (No. C 297) 3 (1980) [hereinafter cited as Vredeling Proposal].

144. Vredeling's portfolio has been assumed by Ivor Richard, Q.C., of the British

impose three distinct obligations upon multinational corporations operating in the European Community. First, MNCs would be required to provide workers' representatives, on a periodic basis, with "a clear picture of the activities of the dominant undertaking and its subsidiaries taken as a whole."[145] This "picture" must include information relating to matters described, all too vaguely, as "the economic and financial situation, . . . the employment situation and probable trends, [and] all procedures and plans liable to have a substantial effect on employees' interests."[146] However difficult it may be to define these terms, what is actually to be disclosed under the Vredeling Proposal would certainly be subject to negotiation and compromise. Few companies would be unwilling to circulate an information sheet to their employees, describing in general terms the present state of the company and its plans for the future.

Second, the Vredeling Proposal would require disclosure of information to workers when "the management of a dominant undertaking proposes to make a decision concerning the whole or a major part of the dominant undertaking or of one of its subsidiaries which is likely to have a substantial effect on the interests of its employees."[147] The parent company must disclose such information to the management of its subsidiary no less than forty days "before adopting the decision,"[148] and it must then be communicated "without delay" to employees' representatives whose opinion must be sought within thirty days.[149] The disclosure must include the "grounds for the proposed decision," its consequences for employees, and "the measures planned in respect of" affected workers.[150] Decisions triggering these obligations include plant closings or transfers, substantial "modifications" to a company's activities or to its organization, and the introduction or termination of cooperation with other enterprises.[151]

Labour Party. Richard was British Ambassador to the United Nations from 1974 to 1979.

145. Vredeling Proposal, *supra* note 143, art. 5, para. 1. References to the Proposal are, unless otherwise indicated, to the published Commission version, pending adoption of a revised text after consultation with Parliament. *See infra* notes 174–177 and accompanying text.

146. *Id.* art. 5, para. 2(b), (d), (h).

147. *Id.* art. 6, para. 1.

148. *Id.*

149. *Id.* art. 6, para. 3.

150. *Id.* art. 6, para. 1.

151. *Id.* art. 6, para. 2.

According to the Commission draft, information about a decision must be disclosed, *before* a decision is formally adopted.[152] This poses a number of potential problems concerning the effect of such disclosure on competition and on share prices and, in the case of U.S. parent companies, raises the prospect that the "insider trading" rules of the Securities and Exchange Commission may be violated.[153] If management must disclose certain future plans to workers' representatives in the EC, this information might arguably be required to be publicly disseminated, in order to prevent insider trading.

Finally, The Vredeling Proposal would require that the consultations with workers' representatives be "with a view to reaching agreement on the measures planned in respect of them."[154] Should the management of the subsidiary fail to carry out such consultations, employees' representatives would be authorized to consult with management of the parent.[155]

The Vredeling Proposal would impose these requirements on parent companies located outside the EC as well as on EC companies.[156] This, however, poses an enforcement dilemma. The EC's writ does not run outside its borders, and although foreign parents might comply voluntarily, provisions for sanctions against enterprises that do not comply might well not be recognized or enforced by non-EC authorities.[157]

The Commission's proposed solution to the problem of enforcement is the "hostage company"provision, which reads as follows:

> Where the management of the dominant undertaking whose decision-making centre is located outside the Community and which controls one or more subsidiaries in the

152. *Id.* art. 6, paras. 1-3. Because of the timing requirements, the decision will not yet have been taken at the time that consultations are opened. The consultation requirement is stated to apply with respect to "the proposed decision." *Id.* art. 6, para. 4. It is probable that workers' representatives could get a court injunction against implementation of a decision as to which they had inadequate or untimely information. *Id.* art. 6, para. 6.

153. Employment of manipulative and deceptive devices, 17 C.F.R. § 240.10b-5 (1981).

154. Vredeling Proposal, *supra* note 143, art. 6, para. 4.

155. *Id.* art. 6, para. 5.

156. *Id.*

157. The Vredeling Proposal provides only that Member States shall provide *appropriate* sanctions for failure to comply with the information disclosure requirements, *id.* art. 5, para. 5, and the consultation requirements. *Id.* art. 6, para. 6. Workers' representatives would be entitled to go to court "to protect their interests." *Id.* There is no comparable enforcement provision purporting to encompass foreign parents.

> community does not ensure the presence within the Community of a [sic] least one person able to fulfil the requirements as regards disclosure of information and consultation laid down by this Directive, the management of the subsidiary that employs the largest number of employees within the Community shall be responsible for fulfilling the obligations imposed on the management of the dominant undertaking by this Directive.[158]

Thus, while the information sought may be located outside the EC, the Vredeling Proposal would require enterprises within the Community to obtain and then to disclose it. By adopting this expedient, the EC would avoid imposing legal obligations directly upon foreign entities.

Even if the "hostage company" provision does succeed in restricting the Vredeling Proposal's obligations to European enterprises, the practical effect of the clause could be more far-reaching. A foreign parent would have two available options before making a decision subject to disclosure and consultation under the Proposal. The parent might designate a person in Europe to consult with workers' representatives, ensuring that this person has been fully briefed on the background of the decision, or it might communicate sufficient information to its largest subsidiary[159] to allow that company's management to conduct the required consultations.[160] In any event, however, the foreign parent must make significant decisions affecting its internal structure, including when and to whom potentially very sensitive information will be distributed within the company.

Although the dissemination of the information required by the

158. *Id.* art. 8. In this and numerous respects, Parliament appears ready to recommend substantial modifications to the Commission text. Thus it is by no means certain that the "hostage company" provision will be part of any directive that is eventually adopted. *See Setback for Vredeling Proposal,* Fin. Times, Oct. 13, 1982, p.1.

159. The Commission text of the Proposal imposes the information and consultation requirements on the largest subsidiary even though it may not in any way be affected by the decision under consideration. *Id.* art. 8.

160. *Id.* Theoretically, there is another possibility: the parent may simply ignore the Vredeling Proposal and allow sanctions to be taken against the management of one of its subsidiaries. Such a course is unlikely because of the harmful effects it would have on confidence in local management and morale in the workforce. It would also raise serious questions about the company's attitude toward its legal obligations.

Seventh Directive[161] and under the periodic disclosure provisions of the Vredeling Proposal[162] would probably not pose problems of sensitivity or confidentiality in the vast majority of cases, discussion of proposed decisions before they are adopted may threaten to compromise important corporate interests.[163] Not only would the security of potentially confidential future plans be in doubt but, in addition, all of the complex commercial and financial relations contingent upon the proper timing of public announcements would be at risk. It is not inconceivable that, under the Proposal, secret designs, marketing strategies, and information on new lines of business could be demanded by employees' representatives.

Many commentators have stressed that the Vredeling Proposal lacks the kind of protections for confidential information that would allow management to countenance its disclosure to workers' representatives.[164] Those gaining access to such information are directed only to treat it with "discretion," and Member States may provide for "appropriate" penalties.[165] Industry spokesmen generally believe that this provision is inadequate, and some fear that con-

161. *See supra* notes 83–111 and accompanying text.

162. Vredeling Proposal, *supra* note 143, arts. 5, 6.

163. *See generally* Continental Oil Co. v. Fed. Power Comm'n, 519 F.2d 31, 35 *cert. denied sub nom.* Superior Oil Co. v. Fed. Power Comm'n, 425 U.S. 971 (1975) (harm to competitive position); Chrysler Corp. v. Schlesinger, 412 F. Supp. 171, 176 (D. Del. 1976) (disclosure of trade secrets and commercial or financial information causing competitive harm).

164. *See* United States Council for International Business, Background Paper: The proposed European Communities' Directive on Worker Consultation and Information Disclosure 4 (Apr. 1981) [hereinafter cited as U.S. Council Paper] (copy on file at the offices of *Law & Policy in International Business*) (The "proposed directive includes no adequate safeguards to prevent proprietary business information from being leaked to competitors. Since confidential information would be communicated to a large number of employee representatives in many countries with conflicting interests, more stringent measures are required to safeguard proprietary company data."); UNICE, Press Release: UNICE Against Proposed EEC Directive Known as "Vredeling Proposal" 2 (Feb. 20, 1981) [hereinafter cited as UNICE Press Release] (copy on file at the offices of *Law & Policy in International Business*) (The proposal lacks "workable safequards for confidential information and [is] likely to increase conflict between shopfloor, managers and the boardroom.").

165. The secrecy provisions of the Proposal are:

> 1. Members and former members of bodies representing employees shall be required to maintain discretion with respect to information of confidential nature. Each must take account of the company's interests in communications with third parties and shall not divulge secrets regarding the undertaking or its business.
>
> 2. Member states shall empower a tribunal to settle disputes with respect to confidentiality of information.

fidential information might be held to ransom by trade union leaders.[166] They note that should such information be disclosed, no sanction could restore their companies to the competitive position they would thereby have lost.[167]

Another frequently voiced objection to the Vredeling Proposal concerns its relation to the Guidelines for Multinational Enterprises adopted by the Organization for Economic Cooperation and Development (OECD) on June 21, 1976,[168] and to the "Declaration of Principles Concerning Multinational Enterprises and Social Policy" of the International Labor Organization (ILO).[169] Both the OECD and ILO statements, adopted with the concurrence of the EC Member States, call for multinational companies to consult with their workers on a voluntary basis, with due consideration of questions of legality, competition, and the overall health of the enterprise.[170]

U.S. business organizations have been in the forefront of those opposed to the Vredeling Proposal.[171] Their principal objections have been those outlined here: the competitive impact of premature disclosure, extraterritoriality, the inadequate protection of confidential data, inconsistency with other international agreements, and the practical difficulties with the disclosure and consultation requirements. They argue that such cumbersome obligations to disclose and consult over decisions of perhaps only tangential relevance to Europe can only make the EC a less attractive place for new or continued investment.[172]

At the very least, compliance with the Vredeling Proposal would

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3. Member states shall impose appropriate penalties in cases of infringement of the secrecy requirement.

Vredeling Proposal, *supra* note 143, art. 15 paras. 1-3.

166. *See* U.S. Council Paper, *supra* note 164, at 5; UNICE Press Release, *supra* note 164, at 9-12.

167. *See* National Foreign Trade Council, Memorandum Concerning Proposed EC Directive on Consultations with Employees 7 (Feb. 19, 1981) [hereinafter cited as NFTC memo] (copy on file at the offices of *Law & Policy in International Business*) ("punishment of offenders could not compensate the corporation for irreparable competitive damage.").

168. For a discussion of the OECD Guidelines, see *Caborn Report, supra* note 78, at 16-18.

169. For a discussion of the ILO Declaration, see *Caborn Report, supra* note 78, at 18.

170. *See* INSTITUTE FOR INT'L & FOREIGN TRADE LAW, THE OECD GUIDELINES FOR MULTINATIONAL ENTERPRISES: A BUSINESS APPRAISAL 129 (1977).

171. *See A multinational bone for Europe's hungry unions,* ECONOMIST, Apr. 24, 1982, at 73.

172. *See generally supra* notes 164, 166, 167 and accompanying text.

be confusing and costly. The draft text of the Proposal does not indicate how to resolve conflicting views between workers' representatives in two Member States, or at two sites in the same State concerning a proposed decision. The Proposal fails to include remedial provisions available to European workers who believe that a company's decision to open a plant in Brazil harms workers in Italy. It does not address the policies of companies which prefer in principle to make decisions at a low level of the corporate hierarchy, as close as possible to the workplace affected.

Perhaps all these criticisms are best exemplified in the position paper of the National Foreign Trade Council: "More broadly, the directive would deter corporate management from innovative changes and initiatives, thereby reducing the productivity and competitiveness of European Community enterprises in comparison with companies in other parts of the world."[173] Granting that such a concern on the part of U.S. industry is not wholly altruistic, neither is it entirely selfish. U.S. companies do, after all, have the option of doing business wherever they deem the atmosphere and opportunities most suitable and accommodating. European companies, governed by the laws of their incorporation and citizenship, often do not have such a choice.

The Vredeling Proposal was sent to Parliament and ECOSOC in 1981, and three parliamentary committees have reviewed it and prepared reports. The Committee on Social Affairs and Employment, which had primary responsibility, has supported an amended version of the Vredeling Proposal.[174] Both the Commission text and the Committee's proposed revisions were laid before the plenary session of Parliament, meeting in Strasbourg in September 1982. The Members of the European Parliament tabled nearly 250 amendments in addition to those contained in the Committee report.

Parliament voted in September, after six hours of debate, to defer detailed review of the Proposal until the October session. In October, Parliament approved a text which contains some significant alterations to the original draft. These include, inter alia, the following:

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173. NFTC memo, *supra* note 167, at 5.

174. *Report on the Vredeling Proposal*, EUR. PARL. DOC. (No. 1-324)(1982) The Committee on Economic and Monetary Affairs and the Committee on Legal Affairs are also producing reports.

1) the minimum size of an enterprise to "trigger" obligations under the Proposal would be 100 employees in a given EC facility *and* 1,000 employees in the group as a whole;

2) workers' representatives must be freely elected by the workforce;

3) in lieu of holding the largest EC subsidiary of a company "hostage," disclosure and consultation obligations would be imposed upon management of the local subsidiary affected by the decisions;

4) the scope of consultation obligations would be clarified;

5) it would be made clear that consultations are limited to the effects of a proposed decision on the workforce, and need not consider the decision itself;

6) it would limit the so-called "bypass" provisions that give EC workers' representatives access to the parent company's management, granting the right to make a written demand for information only when the subsidiary refuses to supply it; and

7) it would exempt business and trade secrets, including information which could have an impact upon share prices, from mandatory disclosure.[175]

The endorsement of such a text by Parliament does not, however, conclude its role in the legislative process. In October, Parliament pointedly declined to adopt a "motion for a resolution," the "vehicle" that transmits the text of a proposed directive to the Council and completes the consultation required under the Treaty of Rome.[176] As of October 1982, therefore, the Proposal still lies before Parliament.

Instead of formally adopting the text and sending it on to the Council, Parliament has asked Commissioner Richard to state his views on the suggested amendments. Richard has the authority to propose modifications of his own,[177] and Parliament appears to want assurances that his changes will not differ substantially from those it has endorsed. Commissioner Richard has undertaken to consult labor and industry groups, among others, and to report back at the

175. *See* Vredeling Proposal as amended by Parliament, Oct. 1982. (copy on file at the offices of *Law & Policy in International Business).*

176. Treaty of Rome, *supra* note 1, art. 54(2).

177. *Id.* art. 149.

November session. He has made no commitment to adopt Parliament's amendments. Among the possible outcomes of this procedure is the exploration of previously uncharted constitutional waters.

As in the case of the Ninth Directive, it is necessary for persons of all ideological persuasions to see the Vredeling Proposal in the appropriate context. Plant closings have been a serious problem in several European countries.[178] Unemployment is reaching catastrophic proportions.[179] The national legal systems of the Member States have been inadequate to prevent these problems. Whether the Vredeling Proposal would ameliorate these conditions is uncertain. What is certain, however, is that there is a very significant movement in Europe which firmly believes that it would.

The debate over the Vredeling Proposal has significant political implications as well. It would be extremely impolitic, given the economic climate, for the EC to deny the trade union movement any remedial measures that might protect jobs. To do so would be to increase the alienation of labor from Community institutions, and to stiffen the resolve of opposition to membership in the EC among such groups as the British Labour Party.

Charter of the "Societas Europea"

In 1970, the EC Commission proposed a regulation[180] recognizing a new form of corporate organization, to be called the "Societas Europea" (S.E.).[181] This proposal has provoked considerable academic discussion[182] in Europe and the United States, but the political process has moved slowly. Parliament has not given its

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178. Britain's unemployment rose in July 1981 for the fourteenth consecutive month to 2.85 million persons, 11.8 percent of the work force. Since the Conservative Party came to power in May 1979, unemployment has more than doubled. N.Y. Times, July 22, 1981, at A19 col. 1.

179. *See supra* note 138 and accompanying text.

180. For a discussion of the difference between a "directive" and a "regulation," see *supra* note 11 and accompanying text.

181. Proposal for a council regulation on the Statute for European companies, 13 O.J. EUR. COMM. (No. C 124) (1970). The proposal was issued with explanatory notes in 1970 BULL. EUR. COMM. Supp. 8/70, *as amended by* 1975 BULL. EUR. COMM. Supp. 4/75 at 11 [hereinafter cited as Draft S.E. Charter]. *See also* Derom, *The EEC Approach to Groups of Companies*, 16 VA. J. INT'L L. 565, 577 (1976).

182. *See* Derom, *supra* note 181.

opinion, and the regulation is probably years away from enactment.

The draft S.E. Charter presents in microcosm many of the concerns seen in the company law harmonization program. It calls for a two-tier board,[183] with worker participation in the supervisory board, comprising, in equal numbers, shareholder representatives, employee representatives, and representatives of "general interests."[184] It regulates company "groups," defined in terms of actual control even in the absence of equity ownership,[185] and would protect outside shareholders and creditors in the manner of the proposed Ninth Directive.[186] As the regulation is currently drafted, non-EC companies could not create a Societas Europea, although their EC subsidiaries could.[187] There would, however, be special guarantees imposed for the protection of outside shareholders when ultimate control of the S.E. was outside the Community.[188]

183. Draft S.E. Charter, *supra* note 181, arts. 62-73a. The company shall be managed by a Board of Management exercising its functions (represent the company in dealings with third parties; confer power on persons to represent the company; close or transfer establishments; modify activities of the undertaking; conduct long-term cooperation) under continuous supervision of a Supervisory Board. Members of the Board of Management are to be appointed by the Supervisory Board, and the Board of Management must submit periodic reports to the Supervisory Board on the management and progress of the company. *Id.*

184. *Id.* arts. 74a, 75a.

185. *Id.* arts. 6, 223. A dependent undertaking is a separate legal personality over which a controlling company is able, directly or indirectly, to exercise a controlling influence. *Id.* art. 6. A controlling undertaking and one or more dependent undertakings shall constitute a group if they are under the unified management of the controlling undertaking and if one of them is a European company (S.E.). *Id.* art. 223.

186. *Id.* arts. 228-239. After a group is formed, the controlling undertaking must offer to acquire the shares of outside shareholders for cash or, where the controlling undertaking is an S.E., in exchange for shares or convertible debentures of the controlling company. In addition, annual equalization payments calculated in proportion to the nominal value of shares must be offered. *See infra* note 188. The Board of Management of the dependent undertaking must report to outside shareholders on the appropriateness of the offer and must convene a meeting to decide whether or not to accept the offer. *Id.* arts. 229-238b. The controlling undertaking would be liable for the debts and liabilities of dependent undertakings. *Id.* art. 239.

187. *Id.* arts. 2-3.

188. *Id.* arts. 228, 231. Where the controlling undertaking is an S.E., it must, upon the formation of a group, offer to acquire the share of outside shareholders for cash or shares, at its option. Where the controlling undertaking is not organized under the laws of a Member State, however, it must offer cash but may also offer to exchange for shares instead. *Id.* art. 228. *See supra* note 186.

When the controlling undertaking offers annual equalization payments, its offer may be calculated as representing the average prospective earnings per share in light of previous earnings and the future prospects of the dependent undertaking. If the controlling under-

The S.E. would be no more than an option available for doing business in Europe. It is envisaged as a kind of "federal corporation," designed to have the maximum flexibility in cross-border dealings within the Community. Such flexibility would endow S.E. companies with a significant advantage, and therefore, non-European industry should carefully follow the emergence of the S.E. concept. Also, because of the similarities between the S.E. charter and the company law harmonization program, developments with respect to the former illustrate the concerns and objectives of EC officials with respect to the harmonization program as a whole.

CONCLUSION

It is essential for non-European business interested in the European Community to see what the company law harmonization program is, and also what it is it is not. The program is conceived as a comprehensive attempt to protect workers, creditors, minority shareholders, and the public against certain risks arising from the conduct of corporations. It is not the opening salvo of a socialist revolution or of major economic warfare with the United States.[189]

Many commentators, including the author of this article, believe that the proposals currently under consideration suffer from serious defects, both in their drafting and in their underlying principles. Many argue that the proposals are inadequately designed to achieve their stated objectives, and that they will neither provide the desired security nor, ultimately, increase employment or economic welfare.[190]

Certainly investment relations between the United States and the EC are not now at their best. Charges and counter-charges of impermissible extraterritorial jurisdiction are frequent. The United Kingdom's Protection of Trading Interests Act 1980,[191] and France's Loi No. 80-538,[192] have been enacted specifically to limit

taking is an S.E., it may calculate the payment by reference to the earnings per share of the controlling undertaking. *Id.* art. 231.

189. *Caborn Report, supra* note 78.

190. *See supra* notes 97-111 (Seventh Directive), 121-142 (Ninth Directive), 164-173 (Vredeling Proposal) and accompanying text.

191. Protection of Trading Interests Act 1980, ch. 11 *in force* March 20, 1980. *See also* Lowe, *Blocking Extraterritorial Jurisdiction*, 75 AM. J. INT'L L. 257 (1981).

192. Law No. 80-538, [1980] J.O. 1799 *reprinted in* Herzog, *The 1980 French Law on Documents and Information*, 75 AM. J. INT'L L. 382 (1981).

the effect of U.S. antitrust laws overseas.[193] Prompted in large part by the Vredeling Proposal, Representative Thomas Luken (D-Ohio) and Senator Steven Symms (R-Idaho) have introduced bills in the U.S. Congress, patterned after the U.K. law, to protect U.S. companies from allegedly extraterritorial EC legislation.[194] The Luken and Symms Bills, both entitled "The Protection of Confidential Business Information Act," would require or permit U.S. businesses subject to foreign regulations that compel disclosure to protect the information sought if it is in fact confidential.[195] The two bills are retaliatory legislation, in that, if either were enacted and had its provisions triggered by a demand for disclosure under the Vredeling Proposal, U.S. and Member State government agencies would immediately be at loggerheads. U.S. companies would, under certain circumstances at least, be directed by U.S. law not to

193. *See supra* note 103. President Reagan's decision extending the ban on dealing with Soviet natural gas pipeline construction to subsidiaries and licensees of U.S. companies has heightened the debate on extraterritoriality. While it does appear that the pipeline sanctions crisis will end amicably with an agreement concerning subsidized trade with the Eastern bloc, many Europeans are angered by this extension of American law to companies incorporated in their countries.

194. The Luken bill would empower the SEC to issue protective orders (generally or at the request of individual companies) against compliance with foreign orders to disclose confidential information. H.R. 4339, 97th Cong., 1st Sess. (1981) (introduced July 30, 1981) [hereinafter cited as Luken Bill]. At present, the Luken Bill is pending in the House Committee on Energy and Commerce, Telecommunications, Consumer Protection and Finance Subcommittee. The Chairman of the Oversight and Investigation Subcommittee is planning an investigation to bring the situation to public attention.

The Symms bill would require U.S. companies to inform the Attorney General when they receive such orders, so that he may direct them not to comply. S. 1592, 97th Cong., 1st Sess. (1981) (introduced Aug. 3, 1981) [hereinafter cited as Symms Bill]. At present the Symms Bill is in the Senate Judiciary Committee. Its sponsors are pushing for joint hearings with the Senate Finance Committee, and are waiting anxiously to see the progress of the Vredeling Proposal. The EC directives are clearly among the intended targets of these measures. *See* 127 CONG. REC. S9230-31 (daily ed. Aug. 3, 1981) (remarks of Sen. Symms). *See also* 127 CONG. REC. H6016 (daily ed. Aug. 4, 1981) (remarks of Rep. Schulze).

195. Section 4(a) of the Luken Bill provides that the SEC shall promulgate regulations protecting U.S. citizens from extraterritorial disclosure requirements affecting such confidential material; section 4(b) empowers the SEC to issue protective orders where necessary; and section 4(c) empowers the SEC to order non-disclosure under certain circumstances. Luken Bill, *supra* note 194, § 4(a)-(c). Section 4(a) of the Symms Bill requires business to notify the Attorney General of any requirement imposed by a Foreign Government for disclosure of confidential information, and section 4(c) empowers the Attorney General to order non-disclosure in certain circumstances. Symms Bill, *supra* note 194, § 4(a), (c).

comply with obligations apparently imposed upon them by European law. The probable resolution of such a conflict is difficult to determine.

In addition, there are currently before Congress several bills to reform section 301 of the Trade Act of 1974.[196] Some of these proposals[197] would enable the President to retaliate against foreign unfair investment practices or against the failure of foreign nations to observe reciprocity in their treatment of investments by U.S. nationals. At least one of the bills has been expressly linked by its sponsors to the Vredeling Proposal and other EC initiatives.[198]

Despite these attempts to retaliate in kind against what may be perceived as over-regulation of business outside national boundaries, it is probable that the European legislative project will continue. The introduction of bills in Congress, however, may well serve the critical function of directing the focus of policymakers on both sides of the Atlantic to the international, and essentially the bilateral, character of the company law harmonization program. U.S. business, with $80 billion invested in Europe,[199] is a major constituent of any program that is responsible for the economic future of the Community.

Resolution of differences of opinion on a bilateral basis will

196. Trade Act of 1974, § 301, *as amended by* The Trade Agreements Act of 1979, 19 U.S.C. § 2411 (1976).

197. H.R. 4407, 97th Cong., 1st Sess. (1981) (introduced by Rep. Richard Schulze (R.-Pa.)), 127 CONG. REC. H6106 (daily ed. Aug. 4, 1981) and the identical Senate version, S. 2067, 97th Cong, 2d Sess. (1982) (introduced by Sen. Symms), 128 CONG. REC. S423 (daily ed. Feb. 4, 1982).

198. It "is of great concern to this country that the European community now plans to hand over the management of business — including American businesses — to trade unions, many of them leftist or Communist dominated.... The so-called Vredeling proposal, now under consideration in the European Parliament, would do exactly that." 127 CONG. REC. H7731 (daily ed. Oct. 26, 1981) (remarks of Rep. Schulze).

"[T]he legislative program of the European Communities [is unfair and unreasonable]. The seventh and ninth company law directives, and the so-called Vredeling proposal, would impose unreasonable and extremely burdensome requirements upon U.S. companies of information disclosure, consultation with trade unions, and even personal liability of U.S. directors." S. 2067 "would insure that. . .the President will be empowered to take retaliatory investment-related measures when other countries discriminate against American investments." 128 CONG. REC. S423 (daily ed. Feb. 4, 1982) (remarks of Sen. Symms).

199. Dept. of Commerce/Bureau of Economic Analysis, [1981] SURVEY OF CURRENT BUSINESS, Vol. 61, No. 8,32, Table 12: U.S. Direct Investment Position Abroad, Year end 1980.

include many aspects: diplomatic contacts between U.S. and EC officials at the appropriate working levels; ready accessibility between EC policymakers and foreign business representatives; maximum transparency of the EC legislative process; and the elimination of harsh rhetoric that inflames passions and dulls reasoning. Non-Europeans must be aware of the important economic and political considerations that underlie the harmonization program; Europeans must recognize that the creation of an atmosphere hostile to business would destroy the kind of cooperative society that the program is apparently designed to create.[200] Each side must be far more receptive to, and understanding of, the legitimate concerns of the other. Such understanding is, after all, the very essence of cooperation, and if the United States cannot cooperate with its oldest and closest allies, the economic future of the Western Alliance seems grim indeed.

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200. The directives and proposed directives considered in this article are by no means the only proposals of the European Community which would have drastic effects upon the operations of non-European multinationals in Europe. The proposed Directive on Liability for Defective Products would establish a system of virtually absolute liability for products which cause injury, regardless of whether the article could have been regarded as defective in light of the state of scientific and technological development at the time the article was put into circulation and regardless of whether the manufacturer knew or could have known of the defect. 22 O.J. EUR. COMM. (No. C 271) 7 (1979). The proposed Directive to Approximate the Laws of the Member States relating to Trade Marks forbids in nearly all cases the use of different trade marks by the same manufacturer for the same product in different Member States. 23 O.J. EUR. COMM. (No. C 351) 2 (1980). Other initiatives would regulate specific industrial sectors, such as banking, pharmeceuticals, insurance, and advertising. There is no indication that the Commission staff is running out of ideas for proposed legislation affecting business.