A Case-Based Approach to Comparative Company Law

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1. Introduction

Two developments in recent years inspired the editors and country experts to come together to write this book on comparative company law. First, the recent financial crisis and economic recession have caused a number of organisations and bodies to re-evaluate various areas of financial, commercial and company law. Evidence emerged which demonstrated the downward pressures of the crisis on the GDP and output of developed economies.1 The shock waves produced by the financial upheavals generated a great deal of soul-searching within the wider commercial and regulatory community with regard to the effectiveness of financial regulation and the general acceptability of corporate behaviour. For example, in a recent consultation paper, the European Commission asked for views on the future direction of EU company law and whether the existing legal framework is fit for purpose or needs to be adapted in light of evolutions in commercial practice.2 This has been mirrored in a number of Member States in the EU3 and further afield, which have questioned the relationship between the managerial board and shareholders of companies, as well as how to best secure prolonged financial stability and the proper functioning of equity markets.

The second driver of this project was the exponential growth in interest in comparative company law in the academic world and the community of legal practitioners. For example, in the period from 2002 to 2011, no fewer than 10 monographs or edited collections were published exploring this new field of enquiry.4 The burgeoning literature

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was mirrored by an increase in university postgraduate courses or programmes in comparative company law and corporate governance. Moreover, the dissolution of trade barriers and mass cross-border capital flows engendered by the forces of competition and globalisation have also necessitated European legal practitioners to be conversant with the company laws of jurisdictions other than their own. As corporate clients expand their interests across a broad portfolio of jurisdictions in a drive for ever greater global efficiency, their legal advisers are required to have some knowledge of each of the legal systems within which they operate.

In producing this work, the general editors and country exports intended to add to the existing academic literature, albeit by adopting a novel methodological approach to the subject. The existing academic literature on comparative company law focuses very much on the institutional structure of the corporation. For instance, discussions centre around whether companies have only one board of directors (‘one-tier systems’) or whether there is a distinction between the management and supervisory board (‘two-tier systems’), whether companies should establish committees (remuneration, appointment, audit committees etc), the identity of persons who can be appointed as a company’s auditor (independence, qualification etc) and the division of powers between the board of directors and the shareholders in general meeting. Whilst this approach is important, it overlooks the dimension of specific cases in company law matters and how the issues arising from disputes are resolved in different jurisdictions. For example, topics related to directors’ liability, creditor protection and shareholders’ rights and duties may best be understood by analysing how carefully designed hypothetical cases would be solved in different countries. An influential case-based comparative methodology is already used by the Common Core project. However, the Common Core only examines private law in a narrow sense (contract, tort etc). Therefore, the principal purpose of this work is to fill a gap in the comparative law literature by adopting a related approach in the field of company law.

The general aim of this project is to identify whether conceptual differences exist between countries in terms of the source, form, style or substance of the legal rules which comprise their company laws. Therefore, it may be possible to challenge arguments developed in the academic literature which posit that the existence of fundamental differences in the protection of shareholders across countries reduces the scope for convergence in company law systems. Furthermore, our project has a public policy dimension since the


5 For example, in the UK, the University of Oxford offers a postgraduate course in Comparative and European Corporate Law, the University of Cambridge a postgraduate module in Comparative Corporate Governance, the School of Oriental and African Studies (SOAS) an International and Comparative Corporate Law course at postgraduate level and King’s College London a postgraduate course in European and Comparative Company Law.

6 See eg P Davies, K Hopt, R Nowak and G van Solinge (eds), *Forum Europaeum on Corporate Boards in Listed Companies* (forthcoming).

7 See IV A, below.

8 See n 4, above for existing works on comparative company law.

9 For references on the convergence debate, see n 11, below.
existence or absence of differences matters for the question of whether formal harmonisation of company law in the EU, or further afield, is necessary, desirable or at all possible.¹⁰

In Part II of this introductory chapter, we concentrate a little more on the aims and implications of our case-based project. This will involve an exposition of central debates in the comparative company law literature and how the cases in this work have the potential to provide useful insights into the relevance and soundness of the arguments advanced in terms of those debates. Part III goes on to provide an explanation of the rationales for drawing up the cases in this book in the way that they have been. In particular, the focus is on the form, style and substance of the cases, within the rubric of the themes of: (1) directors’ liability; (2) creditor protection; and (3) shareholders’ rights and protection and the flexibility of company law. Part IV considers the method and practicalities of adopting a comparative case-based approach, including the mechanics of the process, how the relevant jurisdictions were selected and some of the difficulties encountered by the editors and country experts in designing the cases and furnishing the country solutions and comparative conclusions. Finally, Part V provides a conclusion.

II. Aims and Implications of the Project

One of the principal objectives of this book is to identify and understand possible differences and similarities between legal systems in company law. By identifying the affinities between company law regimes as well as the extent, nature and scope of the disparities, the project has the potential to offer insights into the validity of three of the most central ongoing debates in the field of comparative company law. These debates can be described in shorthand as: (1) the ‘convergence versus divergence’ debate; (2) the ‘legal origins’ theorem; and (3) the legal transplants debate. The relationship between each of these debates is depicted in figure 1.

Each of these debates is cross-cutting and overlaps to some degree, which may be attributed to the fact that each of them at some level addresses the extent to which a single, carefully prescribed framework can ever function as the optimal ‘default operating’ system of company law. For example, stripped to their core, the ‘convergence versus divergence’ and ‘legal origins’ theorem debates concern whether it is practically and normatively sustainable for the Anglo-American company law system to adopt a position of superiority in formal and functional terms. Meanwhile, the legal transplant debate takes as its focus the

adaptability of legal systems to imports borrowed from outside. At this juncture, we now turn to consider how this project will fill a gap and add to these debates.

A. Convergence, Divergence and Corporate Governance Systems

First, this work intends to make a contribution towards the ‘convergence versus divergence’ debate. In 2001, Hansmann and Kraakman wrote a very important article arguing that the US model of corporate law would ultimately ‘win out’ in a competition with civilian systems of company law and that the legal systems of the world would converge to the corporate law regime found in the US. Indeed, certain studies have supplied evidence of such convergence, with a number of factors such as securities law and stock market requirements coalescing to dilute the differences between company law regimes across the world. This phenomenon is partly attributable to the growth of globalisation and, in particular, the pressures exerted by competition, interest groups and imitation. Convergence is not limited to growing similarities between the form, source and style of company laws. Instead, the phenomenon may occur at a number of levels, eg convergence in terms of the function of company law rules (ie rules designed to secure the protection of minority shareholders or

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creditors). Therefore, the evolutionary dynamic predicted by Hansmann and Kraakmann and others is more nuanced and complicated than simply asking whether the form and sources of company laws have converged or are converging.

It is no exaggeration to say that Hansmann and Kraakman’s article generated a reaction amongst comparative company law scholars across the world. Many contested their arguments. For example, some commentators were of the view that the effect of regulatory competition amongst jurisdictions runs counter to convergence, leading inexorably to greater divergence amongst legal systems as each jurisdiction competes and engages in a ‘race to the bottom’ to attract incorporations. Furthermore, cultural constraints, political-economic barriers and the variations one encounters across jurisdictions in the legal rules on the protection of shareholders are other reasons advanced to explain why one ought to be sceptical about the potential for such convergence.

Proponents of ‘path-dependence’ theory argue that the structure of a jurisdiction’s corporate governance system and the shape of its company laws are conditioned by its cultural, social, economic and political past. Hence, ‘history matters’, since once a jurisdiction has embarked upon a particular path, legal systems become ‘locked in’ and conditioned by institutions built up within the system over the years. As a result, strong complementarities between different institutions in the system are generated, rendering it difficult and inefficient for that jurisdiction to suddenly shift direction by introducing an altogether novel set of institutions. For this reason, it is argued that the uniqueness of corporate governance systems ought to be strengthened and permitted to evolve organically in accordance with the existing legal, political, social and economic infrastructure.

In particular, this phenomenon is closely connected with the divergence in the structure of share ownership of companies one finds in common law and civil law countries. In the capitalist market economies of common law jurisdictions such as the UK and the US, which are categorised as ‘liberal market economies’ in the ‘varieties of capitalism’ literature in the field of comparative political economy, the corporate governance system is referred to as an ‘outsider/arm’s length’ system of ownership and control. Ownership of the shares of large public corporations quoted on the capital markets in such systems is widely dispersed with an absence of dominant controlling shareholders. It is argued that the main focus of company laws in such jurisdictions is on protecting the shareholders as

14 For example, a search in Westlaw’s World Journal and Law Reviews leads to 405 citations as at 3 April 2012.
a class from the conduct of managers and directors which is prejudicial to the former’s interests, the latter being in a position to further their own positions at the expense of the former. Furthermore, a large degree of emphasis is placed on corporate disclosure and market control by outsiders. This can be contrasted with ‘co-ordinated market economies’, in the varieties of capitalism literature where the corporate governance system is ‘insider/control-oriented’ in nature. This taxonomy roughly maps onto the company law regimes of the civil law jurisdictions where the share ownership of public corporations is concentrated in a single or a few blockholder controlling shareholders. Such systems are characterised by weak minority shareholder protection, a phenomenon which is largely attributable to the ability of controlling shareholders to extract private benefits by virtue of their dominance and control. Since the governance of companies in such ‘insider/control-oriented’ systems is closely co-ordinated between management and the blockholding controlling shareholders, many commentators contend that company law protections in civil law jurisdictions are designed to protect minority shareholders. The argument runs that the ‘agency costs’ which arise in civilian ‘insider/control-oriented’ jurisdictions are horizontal, ie attributable to a misalignment of the interests of majority shareholders and minority shareholders, rather than a vertical misalignment between the interests of directors and shareholders generally as a class, which is predominant in common law jurisdictions.

In order to understand the possible ‘agency costs’ at play in a company, it is also useful to consider Armour et al, who expound a tripartite division of ‘agency costs’, namely between:

1. directors/managers and shareholders—‘vertical agency costs’, which are prevalent in common law ‘liberal market economies’ such as the UK and the US where shareholdings are widely dispersed;

2. majority shareholders and minority shareholders—‘horizontal agency costs’, encountered principally in civil law ‘coordinated market economies’ such as France, Germany and Italy, where shares are concentrated in the hands of a ‘blockholder’ or a few shareholders; and


22 See Armour et al (n 4).
(3) shareholders and non-shareholder constituencies such as creditors, employees, suppliers, etc.

The debate as to which of the ‘outsider/arm’s length’ or ‘insider/control-oriented’ systems of ownership and control is superior or more efficient has not been resolved: the jury is still out. With its emphasis on case-based problem-solving across common law and civil law jurisdictions, the approach pursued in this book has the potential to test the descriptive relevance of the dichotomy struck in the literature between ‘outsider/arm’s length’ and ‘insider/control-oriented’ systems of corporate governance. If the results of the study point towards the existence of legal techniques in civilian jurisdictions to constrain horizontal agency costs in preference to vertical agency costs, this will furnish some support for the position adopted in the literature. Likewise, if the case-based methodology reveals that common law jurisdictions pay less attention to legal mechanisms whose purpose it is to restrict horizontal agency costs, it will serve to make a contribution to the ‘convergence versus divergence’ debate. The case-based approach is particularly well-suited to such an endeavour, since the solutions to the cases across the selected common law and civil law jurisdictions can be compared and contrasted, with the constituency favoured by each of the solutions duly identified and coded.

B. The Legal Origins Literature and its Critics

A closely related debate revolves around the relevance of the ‘legal origins’ theorem.23 This theorem is connected to the wider notion of ‘legal families’ in the general comparative law literature24 and path-dependency theory considered above. The principal contention advanced by La Porta, Lopez-de-Silanes, Shleifer and Vishny (‘LLSV’) in a series of articles is that corporate law regimes grounded in the tradition of the common law are more protective of shareholders than civilian systems:

Compared to French civil law, common law is associated with (a) better investor protection, which in turn is associated with improved financial development, better access to finance, and higher ownership dispersion, (b) lighter government ownership and regulation, which are in turn associated with less corruption, better functioning labor markets, and smaller unofficial economies, and (c) less formalized and more independent judicial systems, which are in turn associated with more secure property rights and better contract enforcement.25


The argument posits that the direct correlation between regimes which protect shareholders and the sophistication of the state of the capital markets and financial development of a jurisdiction means that civil law countries suffer from a weaker level of stock market development. This has developed into a highly influential body of academic literature, particularly via the Doing Business reports of the World Bank. The ascendancy of the common law position is said to be attributable to a low level of government ownership and regulation of corporations, less formalised judicial procedures and the emphasis it attaches to the reasoned and incremental development of company law through a highly independent judiciary.

For obvious reasons, the ‘legal origins’ theorem has generated a great deal of controversy. The critiques vary from concerns about the failure of the theory to consider the political determinants of corporate law and corporate governance systems to the adequacy of the methodological approach adopted by LLSV and the assumptions that underpin the conclusions drawn from the empirical results. For example, Roe refers to the tendency of governments of a ‘left-wing’ social democratic hue to favour the interests of labour over capital. In such systems, company laws protecting shareholders as a class are eschewed owing to the governmental preference to prioritise the demands of labour, which leads to a greater intensity in conflicts between the interest of shareholders and directors/managers. Greater opportunities arise for vertical agency costs which are attributable to the policy preferences of those ‘left-wing’ governments with a socialist tradition.

Turning to the methodological deficiencies, the finding that robust shareholder rights lead to more effective and efficient capital markets and financial development was reached by LLSV on the basis of a limited range of coded variables and ‘cross-sectional data on the laws of countries in the late 1990s, with no systematic coding of legal change over time’. Studies conducted on the basis of longitudinal time-series coding systems have demonstrated that the evidence for a correlation between legal origins and stock market development is much more tenuous. Moreover, these studies revealed that the level of shareholder protection in civil law regimes has been catching up with common law jurisdictions in recent years.

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26 See www.doingbusiness.org.


30 Armour, Deakin, Mollica and Siems (n 28) 1437–38. Author’s annotations appear in square brackets throughout this chapter.

31 Armour, Deakin, Sarkar, Siems and Singh (n 28).

32 Armour, Deakin, Lele and Siems (n 28).
Turning to the criticism of the assumptions underpinning the findings reached by LLSV, Pistor propounds three fallacies which lie at the heart of the ‘legal origins’ theorem. First, there is the ‘extrapolation fallacy’ whereby an unsubstantiated assertion is made that common law systems with stronger legal protections for shareholders invariably incentivise smaller investors to save their money in shares, leading to a broader investor base and greater capital market development.\(^{33}\) Second, Pistor advances the ‘transmission problem’, which criticises the supposed unidirectional impact of legal origin on specific legal provisions in regulations, statutes and case law and more efficient economic outcomes.\(^{34}\) Here, LLSV fail to address the possible feedback between legal origins, specific legal provisions and stock market development, i.e. reverse causality. Finally, there is the ‘exogeneity paradox’ whereby LLSV assume that a country’s legal origin is exogenous and thus independent of the political, social, economic and cultural context. Instead, there is evidence which shows that the state of a jurisdiction’s stock market and economic development is dependent on a number of factors, including political and economic events and shocks.\(^{35}\)

It is submitted that the case-based approach adopted in this work has the ability to offer some input into the legal origins paradigm. It compares jurisdictions according to whether they are protective of directors, majority shareholders, minority shareholders or creditors in terms of carefully constructed hypothetical cases. Although one cannot go so far as to contend that the findings of such a case-based methodology will operate to reveal the rationales for divergences in shareholder protection across the selected jurisdictions, there is considerable force in the view that it will serve to capture nuances in the level of shareholder protection which the cruder ‘binary type’ methodological approach of LLSV is unable to achieve. Moreover, it has the added attraction of possessing the capacity to expose the differences in the source/form and style of the legal rules which function to confer protection on the various constituencies of directors, shareholders and directors.

### C. Legal Transplants in Company Law

Finally, we move on to consider the relevance of the case-based methodology deployed in this work to the ‘legal transplants’ debate in the comparative company law literature. This debate is also closely linked to the ‘convergence versus divergence’ and ‘legal origins’ debates. The ‘legal transplants’ theory asserts that it is ‘socially easy’\(^{36}\) to lift a rule or system of law from one jurisdiction to another. The theory was developed by Watson in his studies on Roman law. The underlying point made by Watson, which is significant for the project adopted in this book, is that law is an autonomous phenomenon and can be divorced from the social, cultural, economic and political background within which it operates. Instead, the legal tradition, rather than the cultural, social, economic or political context, is more important when it comes to an evaluation as to whether the adoption of a particular rule or body of law by one particular legal system from another (a) ought to be pursued in normative terms and (b) will be successful.\(^{37}\) For that reason, Watson rejects the contention that

\(^{33}\) Pistor (n 28) 1648–56.
\(^{34}\) Pistor (n 28) 1656–59.
\(^{35}\) Pistor (n 28) 1659–62.
contextual features ought to be given wider consideration prior to any legal borrowing for fear that the recipient legal system will reject the transplant. This point is developed further by Cotterrell, who draws a distinction between instrumental law and cultural-based law. Unlike family law, which is conditioned by a jurisdiction’s social and cultural context, and constitutional and administrative law, which is shaped by its political culture, Cotterrell argues that company and commercial law are relatively culturally neutral in nature, since such laws are inextricably linked to ‘economic interests rather than national customs or sentiments’.38 For that reason, company laws are more easily transplantable than family or succession laws and there is less scope for them to be rejected when borrowed by a host jurisdiction with a wholly diverse contextual background from the home jurisdiction.

However, not all scholars are convinced by Watson’s theory. The sceptics can be grouped into two camps, namely the contextualists and the culturalists. First, the contextualists reject the idea that law is an exogenous phenomenon and will be accepted by a host jurisdiction irrespective of its culture and context. For example, Kahn-Freund takes the position that ‘any attempt to use a pattern of law outside the environment of its original country entails a risk of rejection … [and] its use requires a knowledge not only of the foreign law but also of its social and above all political contexts’.39 The difference between the contextualists and the culturalists is a matter of degree, since the latter take the more extreme position that the notion of legal transplants should be rejected outright. The leading proponent of the culturalist argument is Legrand, who asserts that ‘[i]n any meaningful sense of the term, “legal transplants” … cannot happen’.40 Here the argument is that once received, a rule or system of law is no longer comparable to its original incarnation in the home jurisdiction. Instead, the form and style of the rule or system of law is refined and shaped by the local context, environment and culture to the extent that it no longer makes sense to talk of the subject of study as a ‘legal transplant’.

The study adopted in this work seeks to test some of these theories, particularly in light of the Japanese experience and the newly acceded EU jurisdictions of Poland and Latvia. It is often said that the latter two jurisdictions share affinities with the Germanic model of company law, particularly the Latvian legal system, and that the Japanese system imported a number of company law rules from the US following the Second World War. Therefore, the case-based approach employed offers scope to make a contribution to the legal transplants debate. It will do so by reflecting on whether the case solutions offer any evidence of the extent to which formal or functional transplants have succeeded.

### III. Form, Style and Content of Hypothetical Cases

In this book we consider 10 hypothetical cases. These cases were selected in order to cover topics of directors’ duties and liabilities (chapters two to five), creditor protection, including the relationship between creditors and the company (chapters six to seven), and the law relating

40 P Legrand, ‘What “Legal Transplants”? in Nelken and Feest (n 38) 57.
to shares, shareholders, shareholder protection and the flexibility of company law (chapters eight to eleven). Such an approach has the potential to reveal the extent to which the legal systems selected favour the interests of directors, majority shareholders, minority shareholders or creditors. This feeds into the higher-order abstract debates in the wider comparative company law literature on the relevance of legal origins, ‘convergence versus divergence’ and legal transplants, discussed in the previous section. Furthermore, it also has the scope to corroborate or refute the argument that agency costs in common law jurisdictions are oriented towards the minimisation of vertical agency costs and that legally constructed constraints of horizontal agency costs represent the focus of civilian systems of company law.

The view was also taken that some of these questions ought to be addressed to different types of companies. Thus, the aim was to have a good mix of cases dealing with smaller, medium-sized and more substantial companies. Four of the cases asked for a solution based on the applicable law of private limited liability companies. Meanwhile, the remaining six cases concerned public companies (ie joint-stock companies), some of which had their shares admitted to a stock exchange/regulated market. Furthermore, the point should be made that the main focus of the cases in the project is on the company law rules of the countries selected, rather than a comparative examination of the rules of corporate governance. The connection between company law and corporate governance is particularly close. Hence, although the case-based approach adopted may throw some light on certain aspects of corporate governance in the jurisdictions analysed (eg one-tier or two-tier board and the nature, structure and composition of sub-committees of the board), which is revealing or interesting from a comparative perspective, that is not the primary purpose of the project.

In detail, we deal with the following topics, structured in three parts.

A. Directors’ Liability

Turning first to chapters two to five in Part one, which address the position of the 10 jurisdictions in respect of directors’ duties and liabilities, the focus of the first case in chapter two was twofold. It sought to understand the source, nature, content and scope of a director’s duties of loyalty and care, as well as to evaluate the ability of the shareholders in general meeting to authorise or ratify a breach of director’s duty. It is often said that modern jurisdictions adopt the ‘shareholder primacy’ model, whereby directors owe legal duties to shareholders as a class and are bound to run and manage companies in their interests. However, the law in the US (Delaware) amounts to an exception to this general rule and instead prioritises directors’ rights and interests over those of shareholders: this is referred to as the ‘director managerial primacy’ model. The primary purpose of this first aspect

41 See cases in chs 2, 3, 7 and 10, below.
42 See cases in chs 4, 5, 6, 8, 9 and 11, below. The cases on takeover law in chs 4 and 5 concern companies whose shares have been admitted to trading on a stock exchange.
43 See ch 12 at II B, below.
of this case was to test these theories, in particular against the backdrop of the argument that it is most efficient to design company law with a preference for shareholders’ rights and empowerment.46

Turning to the second aspect of the first case, namely the extent to which shareholders may ex ante authorise, or ex post facto ratify, managerial breaches of duty, there is a connection here with the aforementioned ‘shareholder primacy’ and ‘director/managerial primacy’ models. The link relates to the balance of constitutional power between the directors and the shareholders which has been struck by company law: the more power, rights and authority wielded by the directors/managers, the less influence the shareholders have over corporate decision-making and, conversely, the more rights and powers reserved to the shareholders, the more that the directors’ hands are tied in administering the affairs of the company. Therefore, by enquiring as to whether shareholders have the power to absolve the directors of liability for breaches of their duties of loyalty and care, the second aspect of the first case seeks to identify whether shareholders enjoy a residual power or authority over the directors in the context of managerial wrongdoing.

The next case in chapter three moves away from a general consideration of directors’ duties and liabilities to investigate the parameters of the legal obligations of nominee directors and to consider the status of promissory notes which are convertible into equity. Having been appointed by a third party onto the board of the company, eg by a parent company or controlling shareholder of the company, the nominee director is placed in a particularly precarious position. Although the director will be keen to ensure that the company is successful, he or she will also be mindful of the interests of his or her appointer. To that extent, the nominee director’s decision-making is compromised by an inexorable division of loyalties, which will be acutely felt in the case of a decision where the interests of the company and those of his or her appointer clearly diverge. The question which arises is how the legal systems of the 10 jurisdictions under consideration strive to resolve this tension. For example, is the vote/decision of the nominee director ignored where it is taken in the interests of the appointer to the detriment of the company, or is it treated as valid as a matter of course, or valid subject to the satisfaction of certain conditions? These are some of the issues that the first part of this case seeks to address. The second aspect of the case in chapter three involves an assessment of the legal recognition and validity of convertible promissory notes. Civilian jurisdictions are often portrayed as restrictive of shareholder rights and this aspect of the case seeks to test that assertion in the context of a particular security. This is particularly relevant in light of the fact that the conversion of convertible promissory notes often enables a creditor to assume a controlling interest in a company.

The focus of the case in chapter four is also placed on the duties of directors in a particular context where managerial loyalties may be conflicted, namely that of a takeover bid. Here, the interests of the directors of the company which is the subject of the takeover bid may deviate from the interests of the shareholders. For example, the bidder may be minded to remove the incumbent management post-takeover with its own management team in order to improve the company’s commercial performance or its overall efficiency. Although the bid may be beneficial for the existing shareholders, the directors’ personal

and corporate loyalties diverge and they may tempted to engage in activities which are designed to protect and entrench their position as directors. One of the objectives of Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids (‘the EU Takeover Directive’)\(^{47}\) was to place constraints on the power of directors to frustrate takeover bids. It does so by empowering Member States to introduce a ‘duty of neutrality’, namely laws regulating the ability of directors to adopt defensive tactics to a takeover bid within carefully prescribed parameters. Member States were afforded various options in the way they could implement this aspect of the EU Takeover Directive and this case enables a survey to be made of the choices made by the Member States under consideration. It also seeks to identify where the line is drawn between the powers of the directors and the shareholders to take a particular form of defensive action.

Finally, the case in chapter five also takes a takeover situation as its focus. However, unlike chapter four, the principal concern is to identify the jurisdictions which apply pre-emption rights on the allotment and issue of shares by a company. In other words, the question is to what extent a company must first offer a fresh issue of shares to the existing shareholders before it is entitled to issue shares to non-shareholder third parties. This is an important issue in light of the provisions of the EU Takeover Directive, since the sanctioning of a rights issue by management is one of the means by which a takeover bid may be resisted.

B. Creditor Protection

In Part two, we move on to scrutinise the protections afforded to creditors in the company law systems of the various jurisdictions analysed in this work. First, the case in chapter six assesses the ability of a creditor of a bankrupt company to seek recourse against the shareholders or directors of that company. If the country solutions revealed that there was the potential for such liability to arise, the country experts were prompted to specifically identify the juridical basis or bases for that liability. First, the question was posed as to whether a doctrine such as ‘piercing the veil of incorporation’ or some other similar doctrine would permit the creditor to look behind the façade of the separate legal personality of the company to enable it to enforce against the bankrupt company’s directors or shareholders. Moreover, it was intended that the qualifying criteria and conditions for that doctrine to operate be exposed. Second, country experts were asked to consider the potential for creditor recourse against the directors of the bankrupt company via the medium of directors’ duties. Here, the issue was whether the law of directors’ duties placed directors under an obligation to take into account the interests of creditors prior to the company entering, or once the company had entered, into a formal insolvency procedure or process. The concern was also to understand whether more heightened obligations were imposed on directors by virtue of the fact that the company had entered into bankruptcy and whether that translated into the potential for personal liability. Further, it was crucial to understand whether the creditors’ rights could be enforced directly against the director or whether they would have to be enforced by a third party such as an insolvency practitioner appointed over the estate of the bankrupt company when it entered into an insolvency process. In the latter case, the absence of director recourse would mean that the creditor’s

position is somewhat compromised, since it will be reliant on the goodwill of the third party insolvency practitioner to vindicate and enforce its rights.

In the next case in chapter seven, the focus remains on the rights and powers of creditors instantiated through the rules and doctrines of company law. However, this case concentrates on a very technical aspect of company law, namely the operation of the rules which together make up the capital maintenance principle. A capital maintenance principle is found in the domestic company law systems of many jurisdictions and in the Second EU Company Law Directive. The principle strives to ensure that creditors’ rights are safeguarded by prohibiting companies from returning capital to their shareholders through a variety of direct or indirect means. One of the principal rules encountered in many jurisdictions is that a company may only distribute its profits as a dividend to its shareholders on an annual basis if it has: (i) distributable profits; and/or (ii) its net assets are not less than the aggregate of its called-up share capital and undistributable reserves. Not all jurisdictions require (ii) to be satisfied and there is also a degree of divergence displayed in how (i) and/or (ii) are ascertained. For example, some jurisdictions adopt accounting-based models, whereas others proceed on the basis of a solvency-based regime. In the former case, the distribution may be made out of any surplus (a) when the company’s net assets (ie its aggregate assets less its aggregate liabilities) are subtracted from its legal capital as expressed in its distributable reserves or (b) in its accumulated realised profits less its accumulated realised losses. This can be contrasted with solvency-based models where the principal issue is whether the distribution will render the company insolvent in the sense that it is unable to pay its debts as they fall due over an identified sustained period of time. As such, one of the purposes of chapter seven is to isolate which model the jurisdictions under analysis duly apply and to consider the merits and demerits of each.

Chapter seven also goes on to address the extent to which the company laws of the jurisdictions concerned prohibit or constrain the capacity of companies to effect ‘disguised distributions’ of assets to the detriment of creditors, eg by transferring assets to a third party or particular shareholder or shareholders at undervalue or by acquiring assets from a third party or particular shareholder or shareholders in excess of the market value. Once again, country experts were asked to ascertain the doctrinal bases for the imposition or non-imposition of such liability and whether disguised transfers were directly or indirectly precluded or restricted, or whether other legal doctrines operated as functional equivalents and achieved the same result.

C. Shareholders’ Rights and Protections and the Flexibility of Company Law

In Part three, the cases concentrate on the general rights and protections of shareholders and the flexibility of company law. In particular, chapters eight and nine are designed to expose the breadth and limits of shareholders’ rights enshrined in law. For example,

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the case in chapter eight seeks to establish whether shareholders have an entitlement to challenge the decisions of majority shareholders where the latter have failed consistently to vote in favour of the distribution of an annual dividend over a period of time. If the directors and majority shareholders decide to retain profits in the company, the question is whether there are any legal mechanisms enabling the minority shareholders to overturn that decision. The second matter addressed by the case in chapter eight is whether the vote of an interested shareholder in favour of merging the company with another company is somehow tainted and can be ignored on the grounds that it is null and void. Alternatively, one may consider whether that vote is valid, whilst leaving the shareholder open to liability under some other legal doctrine.

Meanwhile, the case in chapter nine looks to understand the circumstances in which shareholders have a right to ask questions of management at a general meeting. Whilst this is an area which has been harmonised in the EU by virtue of Article 9 of the Shareholder Rights Directive of 2007 (Directive 2007/36/EC), a measure of discretion is afforded to Member States to shape the limits of that right, eg by imposing restrictions in order to protect commercial confidentiality and the circumstances in which the shareholder will be deemed to be abusing his or her right to ask questions. Furthermore, this case addresses the legal effect of a purported breach of shareholder rights and whether this operates to invalidate any resolutions passed at a general meeting. In this case, the resolution in question was passed to enable the merger between the company and a third party corporation to proceed. The issue is whether a disgruntled shareholder alleging a procedural violation of company law or the corporation’s constitution has the power to prevent such a merger from proceeding by attaining an order from the court that the merger resolution was null and void.

Unlike chapters eight and nine, which focus on the rights of shareholders, chapter ten seeks to highlight the legal processes recognised in the various jurisdictions which enable shareholders to enforce those rights. Here, the protections of shareholders, particularly minority shareholders, come to the fore. One of the key issues addressed is whether it is possible for an aggrieved minority shareholder to challenge a breach of directors’ duties or the actions of a controlling shareholder through the medium of a derivative action. A derivative action allows a shareholder to attain relief from a director or majority shareholder for the benefit of the company where a corporate decision taken by those directors or the majority shareholders is tainted by self-interest or impropriety, or breaches the company’s constitution or mandatory provisions of national company law. Thus, a successful legal challenge does not give rise to a personal remedy in favour of the shareholder. Country experts were asked to identify the restrictions on the power of shareholders to raise derivative actions, eg whether there were any minimum share capital ownership requirements or whether the genuineness of the shareholder in raising the claim would be considered in advance of a full hearing. This particular case provides the opportunity to consider the theory that civilian jurisdictions prioritise the elimination of horizontal agency costs over vertical agency costs and that common law jurisdictions with widely dispersed ownership seek to achieve the opposite. Chapter ten also seeks to examine the flexibility of the company law regimes of the 10 jurisdictions analysed. Country experts

were asked to consider whether it was possible for a decision to be taken informally by the shareholders with unanimous consent where company law rules or the terms of the company’s constitution specifically required a formal vote to be taken at a properly convened general meeting.

Finally, we turn to the case in chapter eleven whose purpose is to consider whether any legal constraints are placed on the ability of shareholders to restrict the free transfer of shares in the company’s constitution. The possibility of the company conferring pre-emption rights on the transfer of shares in favour of existing shareholders is considered, as well as the ability of the company to restrict a third party from inheriting shares on the occurrence of the death of a shareholder. These two aspects of the case in chapter eleven enable us to address the contention that common law jurisdictions are more flexible than the civil law as regards the structuring and configuration of shareholder rights.

IV. The Method and Practicalities of a Comparative and Case-Based Approach

It is trite to assert the point that a comparative analysis that starts with a particular legal rule, concept or institution soon encounters difficulties if one of the legal systems under observation does not have that particular rule, concept or institution. Thus, many comparatists suggest that one should not start with a particular legal topic but with a functional question, such as a particular socio-economic problem. In the words of Ernst Rabel, it means that ‘rather than comparing fixed data and isolated paragraphs, we compare the solutions produced by one state for a specific factual situation, and then we ask why they were produced and what success they had’. The most striking example of such an approach is the Common Core project, though this has also had its critics, who have challenged the assumptions of the functionalist method. This will be discussed in the first section below. Subsequently, we move on to address the practicalities of our own project, in particular the choice of countries and the procedure applied.

A. The Common Core Approach, its Critics and its Limitations

The term ‘common core’ originates from a project organised by Rudolf Schlesinger at Cornell University dealing with the formation of contracts from a comparative perspective. In the mid-1990s this approach was taken up by European academics interested in contract, tort and property law (now called the ‘Common Core project’). A number of comparative books deriving from this project have been published. In addition, the

52 See the list at www.cambridge.org/gb/knowledge/series/series_display/item3936915/?site_locale=en_GB.
Common Core website and further books provide explanations and reflections on the method used.53

The main idea behind the Common Core project is to draw up hypothetical cases and have country experts describe how these cases would be solved in their legal system. In addition, the organisers of the project explain that they are not only interested in the actual results but also (i) the manner in which different elements of statutory law, case law and scholarly writings interact with and potentially contradict each other in particular legal systems, and (ii) how policy considerations, values, economic and social factors, and the structure of legal processes may affect the solution to the case.54 In some of the books published under the auspices of the project, these two elements appear under separate headings in the solutions.55 However, most case solutions of the Common Core project are focused on the positive law. Thus, the overall approach of the Common Core project is fairly 'legal' and 'practical', which is apparent from the fact that the publisher promotes the series as 'assist[ing] lawyers in the journey beyond their own locality'.56

Short chapter conclusions and separate chapters in the final parts of the books compare the national solutions. This is done in the spirit of functionalism and universalism. The title 'Common Core' is also an overt reference to this aim. Moreover, on the project website it is stipulated that 'in very simple terms, we are seeking to unearth the common core of the bulk of European private law, i.e., of what is already common, if anything, among the different legal systems of European Union member states' and that 'common core research is a very promising hunt for analogies hidden by formal differences'.57 The project website also states that the Common Core approach has an important policy dimension, namely that 'this kind of research should be very useful for and deserve more attention from official institutions that are encharged to draft European legislation' and that part of the Common Core's contribution entails 'building a common European legal culture'.58

According to David Gerber '[t]he value and importance of the Common Core project may well place it among the defining achievements in the history of comparative law'.59 However, this enthusiasm is not shared by everyone; for example, the arch-sceptic Pierre Legrand has dismissed the Common Core publications as 'snippety compilations' that accumulate 'selected titbits extracted largely from legislative texts and appellate judicial decisions'.60

Moving beyond such a polemic, the main criticism of the Common Core concerns the suitability of applying the functional method of comparative law. Critics regard the

53 See www.common-core.org at the main heading 'The Project' (sub-headings 'The Initial Project', 'Approach', 'Answering Questionnaires'); See also M Bussani and U Mattei (eds), Opening Up European Law, The Common Core Project (Bern, Staempfli, 2007).
55 See eg G Brüggemeier, A Colombi Giacchi and P O’Callaghan (eds), Personality Rights in European Tort Law (Cambridge, Cambridge University Press, 2010).
56 See www.cambridge.org/aus/series/sSeries.asp?code=CCEP and www.cambridge.org/gb/knowledge/series/series_display/item3936915/site_locale=en_GB.
57 See www.common-core.org (sub-headings 'The Initial Project' and 'Approach').
58 Ibid.
assumption that all societies face the same social problems as unacceptable. It is argued that human needs are not universal but are conditioned by their environments. This is obvious if one thinks about different natural environments, but it also applies more broadly. The factual situation may be identical in two countries, but this does not imply that the law-makers of both societies will necessarily feel the need to promulgate legal rules on the same issue. Thus, it is said that societies have distinct priorities and that it is unacceptable to impose an external measure on them, such as expecting them all to deal with a particular problem.

Moreover, the very idea that law serves particular functions is challenged. A strict version of functionalism has to assume that there is a clear sequential order: a social problem arises, courts or legislators respond to it, which in turn has the effect of solving the problem. Yet, such a view fails to consider the possibility that legal rules often arise in a complex process of historical path-dependencies, cultural preconditions and legal transplants, and that legal rules also shape the problems of society. It is also not at all untypical that law operates to serve more than one explicit function alone. Law-makers may have responded to conflicting aims or they may simply strive to offer a clear legal framework, being largely indifferent as to how it is used.

Where does this leave functionalism? Some of these points raise important objections: for instance, functionalism may not work well in all areas of law or with respect to legal systems where we cannot say that the law has a well-defined purpose. Nevertheless, it is also submitted that these objections do not discredit functionalism as a whole. Indeed, we hope that this book shows that using hypothetical cases offers important insights into the field of comparative company law. It may also be seen as providing evidence that practical problems in company law are not so diverse across the 10 countries selected to make a case-based comparison worthwhile.

Nevertheless, we do not deny that the case-based approach adopted in this work possesses certain inherent limitations. For example, it is unlikely that such an approach will be useful in evaluating technical issues of company law such as the content and design of the rules on the composition of board membership, the drafting of prospectuses or the transparency of securities markets. The same applies for topics of transnational company law, such as the operations of cross-border and transnational corporations, corporate group structures and cross-border mergers and acquisitions, since a case-based approach is typically focused on the laws of a selected number of countries.


64 This approach will be explained further in M Siems, Comparative Law (Cambridge, Cambridge University Press, forthcoming) ch 2.
B. The Choice of Countries—and the Problems to Overcome

In accordance with one of the objectives of the project identified above, ie whether formal harmonisation of company law in the EU, or further afield, is necessary, desirable or at all possible, the main focus of this study is on the Member States of the EU. However, owing to constraints of space, it was not possible to cover the law of all 27 Member States. Therefore, the focus is fixed on the most populated countries (Germany, France, the UK, Spain, Italy and Poland) as well as a smaller and a newly acceded Member State (Finland and Latvia). In addition, the laws of two of the largest economies of the world, the US and Japan, have been included. This is important and interesting from a comparative perspective since the US is the most important ‘exporter’ of corporate governance theories and ideas, and Japan’s company law is comprised of a mixture of different legal traditions, having had a number of legal transplants over time. It should be clarified that the law of the US state of Delaware was used as a proxy for the US. This is attributable to the fact that Delaware corporate law is the most important and influential in the US, with a significant number of public and private companies incorporated in that state.65

It would also have been interesting to include further jurisdictions from Asia, America or Africa, for instance, some of the BRICS countries (Brazil, Russia, India, China or South Africa) or possibly even ‘radically different legal cultures’.66 However, apart from logistical problems, there are good reasons to focus on relatively similar developed countries. This is related to the feasibility of a functional approach to comparative law. Insofar as the approaches adopted by countries are relatively similar, it is likely that their law-makers regard the same socio-economic problems as legally relevant. It has also been said that a preference for similar countries has the advantage of controlling for the stage of development, ie making it easier to explore the remaining differences amongst a baseline of similarity in terms of the countries’ history, society, economy and ideology.67

Nevertheless, some problems have to be overcome. It was mentioned previously that we aimed to have some cases applicable to private limited liability companies (such as the Ltd in the UK and the GmbH in Germany) and others to public companies (such as the plc in the UK and the AG in Germany).68 However, we encountered the problem69 that the form a company takes does not always correspond with the way it is used in practice. For example, on the surface, the French SARL resembles the German GmbH, and the French SA the German AG, but in France, even small to medium-sized firms and family firms often use the SA. In addition, French law offers a third legal form, the SAS, which was created to cover the area between the SA and the SARL.70 A somewhat analogous situation exists in the US. Here, a primary distinction is made between closely and publicly held corporations, but businesses can also establish a limited liability company (LLC). The success of

68 See III pr, above.
69 For the following, see Siems (n 4) 10–14.
70 See ch 10 at II C, below.
David Cabrelli and Mathias Siems

state LLC laws is particularly based on the fact that while LLCs have the legal form of a company, for tax purposes they are treated as a partnership. In 2005 Japan also introduced the LLC based on the US model, but without the advantage of being taxed as partnerships. By contrast, the UK law provides for a Limited Liability Partnership (LLP) which, like US LLCs, is structured similarly to a company but is taxed as a partnership. 71

The implication of this for the case-based project was that whilst guidance was provided to country experts on the type of company that it was expected would be covered in the individual case studies, some contributors indicated possible alternative solutions for different types of companies. 72 On occasion, country experts also mentioned that a particular aim could not be pursued by adopting the form of company prescribed in the scenario in question, but that another form of company would be available. 73

A more general problem may have been that the solutions received from the contributors often differed considerably in terms of structure and style. For example, some of the solutions provided a precise structure with many headings and sub-headings, whereas others provided a more discursive text. Some referred to many cases and statutory provisions in the text, whereas others only referred to them in the footnotes, often more sporadically. There were also marked variations in the extent to which contributors translated certain terms into English or in the frequency of references to international, comparative and European materials.

An attempt was made to approximate the presentation of the solutions in some instances. However, deliberately, a template was not provided as to how it was anticipated that the solutions would be written and structured. Comparative lawyers often emphasise that it is differences in legal style, not substantive rules, which are decisive for the common/civil law divide. 74 Thus, to some extent, this book has the secondary aim of exposing these differences in legal thinking and writing. However, this point should not be stretched too far. For example, if a particular section contains many references to the academic literature, this may be an indicator of the civil law tradition, but it could also be influenced by the individual style adopted by the contributor in question.

C. The Modus Operandi of the Project

The project was co-ordinated by the two general editors who appointed one or two country experts for each of the 10 jurisdictions under examination. The topics of each of the 10 hypothetical cases were selected by the two general editors, but the issues to be addressed in each case were loosely configured around the topics of directors' duties, creditor protection, shareholder's duties/liabilities and the flexibility of company law and its enforcement. Each of the country experts performed three tasks. First, he or she drafted one hypothetical case and a solution to that case according to the company law of his or her home jurisdiction. The decision to enable each participant to draft one of the cases was predicated on the perceived need to achieve a good mix and balance of cases, possibly reflecting different

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72 See eg the French solutions in chs 7, 10 and 11, below.
73 See eg the German solutions in chs 3 and 11, below.
74 See eg Zweigert and Kötz (n 24) 63–73.
socio-economic circumstances. Second, each of the country experts then circulated their hypothetical cases and solutions amongst the other country experts and solutions were produced by each of the country experts to the hypothetical cases under the law of his or her home jurisdiction. Third, each country expert examined the different solutions to his or her hypothetical case and drew up a comparative conclusion. Once again, the two editors were not overly prescriptive of how the country experts should approach the task of writing the case conclusion. The comparative conclusions would identify the differences and similarities between the 10 jurisdictions and would also provide a careful comparative analysis. In particular, the following issues were addressed in the case conclusions and comparative evaluations where this was possible in light of the hypothetical case and the solutions:

1. Is it the case that formally different legal rules in the jurisdictions lead to functionally similar results? Conversely, are the rules in the jurisdictions formally similar (due to legal transplants etc) but applied differently? On a similar note, is there any evidence of increasing formal or functional convergence and is such convergence desirable bearing in mind (a) the ostensible differences in the form of company laws in jurisdictions according to whether they are grounded in the civilian or common law traditions and (b) the differing shareholding structures in jurisdictions?

2. Is there any evidence that the legal origins theorem (from the viewpoint of the degree of shareholder protection) is relevant and/or applicable, ie is the level of shareholder or creditor protection lower in civil law countries in comparison with common law countries?

3. What are the sources of the legal rules in the jurisdictions examined, ie are they based on case law or statute law (which may or may not relate to the common law/civil law divide) and how is that significant (if at all)?

4. Whether politics or history/path-dependence matters, ie to what extent is there any evidence that politics and/or path-dependence and legal-institutional complementarities influence the form and shape of company laws in different legal systems?

5. To what extent does the nature of the shareholding structure (concentrated versus dispersed and outsider versus insider) in differing countries influence the form which the company laws take?

6. Country experts were asked to reflect on whether the solutions offer any insights into the legal transplantability of company laws, ie to what extent there was evidence of formal or functional transplants having succeeded.

7. Is there evidence to demonstrate that the legal systems predominantly favour one constituency over another, eg directors, managers, shareholders, creditors, employees, etc?

8. Policy questions ought to be addressed, for instance, which solution (if any) may be superior and whether the differences may call for substantive/formal legal harmonisation or functional legal harmonisation.

9. If the case related to directors’ duties and liabilities (ie a case in chapters two to five in Part one), country experts were asked to consider the following factors and address them if they were relevant:

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75 But see III pr and A, above, for functionalism and its critics.
(a) In what circumstances does directors’ liability arise?
(b) Which legal tools are used in order to prevent self-dealing transactions of directors?
(c) Does directors’ liability lead to a damages or disgorgement of profits remedy? Can third parties dealing with a director in breach of duty to the company be held liable to the company?
(d) Are directors/managers/board members jointly responsible?
(e) Are there different standards of care for different members of the board? Are ‘nominee’ directors permitted?
(f) Can shareholders ratify any action, decision or omission of a director and thus prevent the company from litigating against that director?
(g) Can shareholders challenge the remuneration of directors/managers/board members and/or executives?
(h) Is there a duty of neutrality in the case of takeovers and, if so, how and when does it arise?

(10) If the case related to the relationship between creditors and the company (ie a case in chapters six to seven in Part two), country experts were asked to consider the following factors and address them if they were relevant:
(a) Do directors owe a direct or indirect (eg via a liquidator, administrator or other insolvency practitioner) duty to the creditors of the company?
(b) Do directors owe ‘wrongful trading’ obligations to creditors—ie do directors owe a duty not to continue to trade where there is no reasonable prospect of the company avoiding going into insolvent liquidation? If not, are there any circumstances in which the law will impose personal liability on directors whose companies have been dissolved or liquidated?
(c) Is there a concept of ‘piercing the corporate veil’? If so, in what circumstances will it be applicable?
(d) Is there a subordination of shareholder loans in the case of a company in crisis?

(11) If the case related to the law relating to shareholders and shareholder protection (ie a case in chapters eight to 11 in Part three), country experts were asked to address the following factors if relevant:
(a) Can shareholders vote in their self-interest?
(b) Do shareholders have to take the interests of other stakeholders into account?
(c) Do controlling shareholders have special duties? If so, to whom?
(d) Are shareholders’ agreements—for instance, on voting rights—possible?
(e) On what grounds (if any) can shareholders challenge a decision or resolution of the general meeting?
(f) Is it necessary that the general meeting decides about ‘de facto changes’ of the company (eg the sale of substantial assets)?
(g) Is it possible for a shareholder to take action against a director, majority shareholder or other third party to recover a loss sustained by the company? If so, in what circumstances?
(h) Is it possible for a shareholder to sue the company or its managers or controllers where it has been conducted in a manner which is contrary to the interests of that shareholder or the shareholders generally?
(i) Are there any limitations on the ability of shareholders to restrict the free transfer of shares?
(j) Are there any restrictions on convertible corporate bond-holders converting their debt into equity and assuming a controlling interest in the company?
V. Conclusion

The main aim of this book is to identify and understand possible differences and similarities between legal systems in company law. To that end, this chapter has set the scene by explaining how a case-based approach to company law can be used in a fruitful way. We have outlined core topics of comparative company law, such as the debates about convergence of corporate governance systems and the role of legal origins, and how they are addressed in this book. We have also explained more precisely the principal topics that we cover and the practical problems a case-based approach to comparative company law must overcome.

Following the 10 case studies, the concluding chapter76 will revisit the general themes explored in this introduction. As such, it will not only be possible to conclude how countries differ in terms of substantive legal rules, but also whether they use similar or different sources of law, and whether they tend to favour the interests of shareholders, directors or creditors in company law. Despite this overarching aim, the case studies of this book can also be used separately and it will also be clarified at the outset of the chapters how they relate to other topics addressed elsewhere in this book.

The structure of the country solutions is as follows: in order to achieve consistency, the first solution is always from the contributor who produced the case in question. This is followed by the other countries of the same legal family, starting with the jurisdictions, such as France, Germany and the UK, that may have borne an influence on this.77 Subsequently, the solutions of the countries of the other legal family are presented. Japan follows as the final solution, since its company law has been both influenced by the civil and common law legal families. Of course, this order does pre-empt the view that there are telling differences between civil and common law jurisdictions in the field of company law; indeed, the chapter conclusions often highlight, and try to explain, unexpected similarities and differences.

76 See ch 12 below.
77 Thus, our default order of countries is France, Germany, Italy, Spain, Finland, Poland, Latvia (for the civil law) and the UK and the US (for the common law).