EUROPEAN MODEL COMPANY ACT (EMCA)

CHAPTER 16

GROUPS OF COMPANIES

PART 1
DEFINITIONS

Section 1 Definition of a group
Section 2 Definition of parent and subsidiary
Section 3 Definition of a wholly-owned subsidiary
Section 4 Definition of control
Section 5 Criteria of legal control
Section 6 Criteria of factual control
Section 7 Calculation of participation
Section 8 Duty to disclosure control

PART 2
GROUP MANAGEMENT

Section 9 Right of a parent company to give instructions to the management of a subsidiary
Section 10 Right to access information at the level of the subsidiary
Section 11 Right to squeeze-out

PART 3
PROTECTION OF SHAREHOLDERS OF THE PARENT COMPANY

Section 12 Right of access to information and to request a special investigation

PART 4
PROTECTION OF SHAREHOLDERS OF THE SUBSIDIARY

Section 13 Corporate opportunity within a group
Section 14 Right to request a special investigation
Section 15 Right to sell-out
Section 16 Interest of the group
Section 17 Wrongful trading

Chapter 16 Groups of Companies is subject to a public consultation: http://law.au.dk/emca
Introduction

1. Groups of companies are a major economic phenomenon. Since the middle of the last century, enterprises have increasingly chosen to organize and to conduct their business activities in the form of a network of individual separate companies rather than as a single corporate entity: therefore, the group of companies – and not the single company – is the prevailing form of the modern enterprise.

2. As a legal phenomenon, groups are also a very well-known and established topic in several sectors of the law, either in a national or in a European context, e.g., tax law, accounting law, competition law, labour law, and so on. Yet, its treatment in the area of Company Law has proved to be a difficult, disparate and mostly unsolved issue.

There is no specific regulation on groups by European Union law. In fact, the proposal of a ninth directive, which was largely inspired by German law, was dropped by the end of 1980s’, due to the lack of support for this approach.

At the national Member States level, there are four major approaches: comprehensive regulation, partial regulation, a case law recognition of the interest of the group, and lack of treatment (except what is required by EU directives).

The first approach consists in a global and comprehensive regulation of groups of companies. This approach originates in Germany (1965), and has been followed suit closely by Portugal (1986), Hungary (1988-2012), Czech Republic (1991-2012), and Slovenia (1993). It can be noted that this approach has also been adopted in Croatia (1993) and in Albania (2008), and, outside Europe, it influenced also countries such as Brazil (1976). Spain considered adopting a similar regime in 2002, but that attempt failed. However, a new proposal has been introduced in Spain in 2013. Austria and

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3 José Engrácia Antunes, Os Grupos de Sociedades, Almedina, Coimbra, 2002.
7 See proposal of Código de Sociedades Mercantiles, Pablo Girgado, Legislative Situation of Corporate Groups
Poland, although being very close in legal tradition to Germany (like all other countries who adopted the German approach), chose not adopt it.

A second approach consists in a partial or selective regulation, which deals with some major questions of groups of companies without aiming, however, to regulate it in a complete and comprehensive manner. This is the case of Italy which adopted a new regime for groups in 2003. Italian law recognizes the interest of the group. It is influenced by German law but is considered to be more flexible.

The third approach is the French one. It derives from the 1985 Rozenblum decision of the French Supreme Court. In that decision, the court recognized the interest of the group. As a consequence, the directors of a subsidiary may take into consideration the interest of the group when making a decision that prejudices the subsidiary, provided several conditions are satisfied. This flexible approach is recognized in other Member States (Belgium, Luxembourg, Netherlands, Nordic countries).

Finally, some Companies Acts ignore the group altogether. They have no provision, except for those which are imposed by EU directives. This approach is followed for instance in the United Kingdom (UK). However, in the UK, it should be reminded that directors of a subsidiary are able to take into account the interests of the group in making their decisions. The risk of unduly favouring the parent is mitigated by the risk of the subsidiary director’s personal liability for wrongful trading. From a functional perspective, the British approach might not be very different from the French one.

3. The “Forum Europaeum on Group Law”, composed of a group of Academics, published in 2000 a proposition for a European regulation of groups of companies based on some standards and rules – entitled “The Corporate Group Law Principles and Proposals”. This proposal was influenced by German law (“Konzernrecht”), although the drafters moved away from the system put in place in 1965. It was also influenced by French case law (the so-called “Rozenblum” doctrine), and by French and UK law (“obligations aux dettes”, wrongful trading). The starting point and aim of

9 See Peter DORALT and Christoph DIREGGER, in Peter DORALT, Christian NOWOTNY and Susanne KALSS, Kommentar zum Aktiengesetz, Band 2, Linde Verlag (2012) § 15 paragraph 5.
the Forum Europaeum was, to a certain extent, different from the one of EMCA, since the goal was to adopt a European Community solution, and not a national Act. Therefore, once the basic standards were set, many points were left to Member States discretion and option were offered. The proposal of the Forum Europaeum was not adopted at the EU level, due apparently to a lack of support by professionals, at the time, for such regulation\textsuperscript{14}. However, the work of the Forum Europaeum has been used as a basis for the EMCA chapter on Groups.

4. The group of companies, being an economic reality and being also dealt with in many other legal branches, should be also recognized and regulated by Company Law. However, the EMCA should not be addressed to develop a global and systematic legal regulation for groups, based on a rigid conception of the autonomy of the single company and aiming basically at the protection of subsidiary companies, its minority shareholders and creditors. Instead, the main objective of the EMCA chapter on Groups of Companies is to establish a cluster of rules aiming to facilitate and enhance the flexibility of the formation, organization and functioning of this leading form of business organization in nowadays.

The EMCA Chapter on groups is therefore focused on the heart of the group reality: the management of the group. Protection of subsidiary companies and related interests (shareholders, creditors) should not be ignored, of course, but it should not be achieved through by excessively burdensome rules. Moreover, the Chapter also pays a special attention at the level of the parent corporation. It complements the traditional “bottom-up” approach of groups of companies (exclusively focused on the subsidiary or dependent companies) by a “top-down” perspective, which takes also into account the effects of the group at the level of its parent corporation. Likewise, the regulation distinguishes between wholly-owned and not wholly-owned subsidiaries, as protection is less necessary in the former case and the functioning of the group should be as flexible as possible. Finally, the EMCA chapter on groups takes also into account the international nature of many group.

5. In order to reach these general goals the EMCA chapter on groups includes the followings main principles and rules:

A) In order to enhance and facilitate the functioning of the group, the Chapter proposes that:

- the right of a parent company to give instructions to a subsidiary is recognized, without creating a specific liability or burden on the parent company, as this power corresponds to reality. Companies Acts which entitle the parent company with a legal power of direction over subsidiaries only on the condition that an over-reaching protection is granted to creditors, minority shareholders and the subsidiary itself, have proven to provide a legal regime which is deemed to be too rigid and with a relatively scarce practical efficacy.

\textsuperscript{14} EU consultation in 2006: “Consultation on future priorities for the Action Plan on Company Law and Corporate Governance”. 


- the right to manage the group and its constituent members in the interest of the group is also recognized. The EMCA Chapter on groups is inspired by the Rozenblum doctrine. This will provide protection for the management of the parent and subsidiary company against liability (civil and criminal), under certain conditions, when they manage the companies as one entity, which is the reality of a group

- the right to squeeze-out minority shareholders is accepted within a group

- the international dimension of the group, where applicable, is recognized

- intra-group transactions: related party transactions are subject to approval by the board of directors in the EMCA. This follows the UK approach. Therefore, exemptions from approval by the general shareholders’ meeting of intra-group transactions are not needed in the EMCA Chapter on Groups.

B) The protection of minority shareholders and creditors at the level of the subsidiary company is assured through general provisions, like in the United Kingdom, with some specific rights:

- as to minority shareholders: sell-out rights (US appraisal rights)

- as to creditors: introduction of the «wrongful trading».

C) The protection of shareholders at the level of the parent company is also taken into account, namely:

- by consecrating special mechanisms aiming to ensure and enhance the right of information of parent’s shareholders over the subsidiary affairs
PART 1
DEFINITIONS

Section 1
Definition of a Group

A group is the entity comprising the parent company and all its national and foreign subsidiaries or entities, unless otherwise indicated.

Comments

In a comparative perspective, the definition of a group has been mainly construed on the basis of two different concepts. One is the concept of «unified management» (e.g., Section 18 of German Corporation Act). The other is the concept of control (e.g., section 1159 (1) UK Companies Act, section 7 of Danish Company Act, section 12(1) of Finnish Company Act, article 22 of the Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, etc.).

The EMCA definition of group of companies adopts the latter view. The definition was inspired by the pre 2011 version of IAS 27 Consolidated Financial Statements and Accounting for Investment in subsidiaries and IFRS 10 Consolidated financial statements which replaced IAS 27 and has been endorsed by the European Commission. The notion of control is the basis for consolidation in IFRS 10 as it was in the pre 2011 version of IAS 27.

The term company in «parent company» refers to the definition of «company» in the EMCA. A natural person cannot be a «parent company».

The parent company is a national company unless otherwise indicated.

Because of the reference to «all its national and foreign subsidiaries», the term «subsidiaries» in this chapter includes both national and foreign companies, unless otherwise provided. Most Companies Act do not refer to foreign subsidiaries. One exception is Finnish law which refers to «national and foreign» subsidiaries.

15 IAS 27 has been renamed Separate financial statements.
17 Finnish Limited Liability Companies Act §, Section 12 — Group "(1) If a limited liability company exercises control over another domestic or foreign corporation or foundation, as referred to in chapter 1, section 5, of the Accounting Act, the limited liability company shall be the parent company and the other corporation or foundation a subsidiary. The parent company and its subsidiaries form a group".
The definition of the group, or parent and subsidiary (See. Section 2) applies in this chapter and in all the EMCA, unless otherwise provided.

Section 2
Definition of parent and subsidiary

A “subsidiary” is a company subjected to the control, as defined in sections 5 and 6, of another company, the “parent” company, either directly or indirectly through another subsidiary.

Comments

Several Companies Acts refer to the concept of control as the core concept of the definition of «group» or of the parent-subsidiary relationships (section 1159 (1) UK Companies Act, section 7 of Danish Company Act, section 12(1) of Finnish Company Act, section 42 of Spanish Commercial Code). The same happens with article 22 of the Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.\(^\text{18}\)

Other member states have a definition of subsidiary which is limited to holding more than 50 % of capital or votes (eg : Art. L. 233-1 of French commercial code). This approach seems too restrictive. A company should be considered a subsidiary as soon as it is controlled.

Control may be held by the parent company over a subsidiary either directly or indirectly. Companies are affiliated if one is a subsidiary of the other or both are subsidiaries of the same company. The term « affiliated companies » (or the UK Companies Act « associated companies ») is sometimes used in companies Act but is not predominant. Therefore, it is not used in the EMCA itself since rules for affiliated companies can be applied by using the term subsidiary or member of the group.

\(^{18}\) This directive replaced the 7th Directive of 1983 on Group Consolidated Accounts.
Section 3

Definition of a wholly-owned subsidiary

A “wholly-owned company” is a company with no other shareholders except its parent company or any other subsidiaries or persons acting on its behalf.

Comments

A definition of wholly-owned subsidiary is useful since, in the absence of minority shareholders, more flexibility should be allowed in the operations and the management of the group. This definition is limited to companies whose capital is owned at 100 % by the parent company, either directly or by other 100 % owned companies.

This provision is inspired from the UK companies Act (Section 1159 (2) UK Companies Act).

Section 4

Definition of control

Control is the power to govern, alone or with other shareholders, the financial and operating policies of a subsidiary. It may be de jure or de facto.

Comments

This definition is inspired by the pre 2011 version of IAS 27 Consolidated Financial Statements and Accounting for Investment in subsidiaries19. For instance, Danish law has also adopted the definition from IAS 27 with the exception of the sentence «so as to obtain returns from its activities». This term is also excluded from the EMCA Chapter on groups due to the fact that it is an economic concept.

The willingness to hold the shares for the long term or not should not be taken into consideration in order to decide whether or not there is control.

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19 IFRS 10 replaced « benefits », used by the pre-2011 version of IAS 27, by « returns », « because many interpret 'benefits' to imply only positive return. 
Section 5
Definition of de jure control

Control of a subsidiary exists where a company owns, directly or indirectly, more than half of the voting rights in that subsidiary, unless, in exceptional circumstances, it can be clearly demonstrated that such ownership does not constitute control.

Comments

The definition of de jure control is inspired by the pre 2011 version of IAS 27 Consolidated Financial Statements and Accounting for Investment in subsidiaries. The owning of majority of votes is also considered in most Company Acts as a criterion for the assessment of control over a company (e.g., Czech Republic, Denmark, France, Germany, Poland, Portugal, Slovakia, Spain). In some countries, the presumption of control linked to majority voting rights it is irrefutable (e.g., Czech Republic, France, Poland) where in others it is refutable (e.g., Denmark, Germany, Portugal,).

The organization of control in two different articles facilitates the identification by outside parties of the basis of the control.

Section 6
Definition of de facto control

Where one company holds half or less than half of the voting rights in another company, control exists if the former has

1. the right to exercise more than half of the voting rights by virtue of an agreement with other investors;

2. the right to control the financial and operating policies of a company under any articles of association or agreement;

3. the right to appoint or remove the majority of the members of the supreme governing body, and this body has control of the business; or

4. the right to exercise the actual majority of votes at general meetings or an equivalent body and thus the actual control of the business. Control is presumed when a majority of the members of its supreme governing body has been designated by another company for two successive financial years. The other company is deemed to have effected such designations if, during that financial year, it held a fraction of the voting rights greater than 40%, and if no other shareholder directly or indirectly held a fraction greater than its own.
Comments

In subsection 1, the term «power», used by the pre 2011 version of IAS 27 Consolidated Financial Statements and Accounting for Investment in subsidiaries, has been substituted by the term «right», as it is more usual in Company law and is not an economic term”

In subsection 3, the supreme governing body is the board of directors of companies having a board of directors, the executive board of companies having only an executive board, or the supervisory board of companies having both an executive board and a supervisory board.

The right to appoint a majority of the members of the supreme governing body, despite not having a majority of the votes, can originate, from the specific structure of the company (e.g. simplified joint-stock company [SAS] in France) or from law.

In case the right to appoint and to remove is not held by the same persons, control will be deemed to be exercised by the person who can remove the members of the supreme governing body.

Regarding subsection 4,, presumptions should play a major role in defining the existence of a factual control as some companies might want to pretend that they are not controlling another company. Therefore, the burden of proof should be reversed in a way that it should be up to that company to allege and demonstrate that it does not have control. The first and second presumption originates from the Directive 2013/34/EU of 26 June 2013 and French law (Commercial Code, art. L. 233-16).

The definition of factual control, adopted in subsection 6, is inspired by the pre 2011 version of IAS 27.

Section 7
Calculation of Participation

(1) For the calculation of the voting rights pursuant to sections 5 and 6, are also to be considered the rights to subscription and purchase of shares carrying voting rights that are currently exercisable or convertible.

(2) Any voting rights attaching to shares owned by the subsidiary itself or by its subsidiaries must be disregarded in the determination of the voting rights in a subsidiary held by the parent company.
Comments

Similar provisions are found in Germany (Section § 20, par. 2 of German Corporation Act), Denmark (section 7 (4) of Danish Company Act), etc. The consideration of the so-called future or potential voting rights is also common in capital market laws, relating to the disclosure of significant shareholdings. However, there are several Companies Acts which do not take into account this potential capital (e.g. France).

Paragraph (2) is necessary, because otherwise the real controlling influence of the parent company would be underestimated.

Section 8
Duty to disclose control

(1) The management of the parent company must inform in writing the management of a subsidiary as soon as control has been established or removed.

(2) As soon as it is informed, the subsidiary, unless it is a foreign subsidiary and such obligation is not recognized by the law of the country whose rules apply to the subsidiary, must inform without delay the parent company of the number of shares and voting rights held by it in the parent company, and in any other companies.

Comments

Concerning paragraph (1), it is necessary for a subsidiary company to be informed of the acquisition or the end of control by the parent company, so that the former knows its legal situation, since certain rules apply only to controlled companies. Moreover, this written declaration or notification could also operate as a sort of publicity or transparency for groups of companies, since the existence of a group is based on a control linkage between parent and subsidiaries. This type of provision can be found in some national Companies Act (e.g., section 134 of the Danish Company Act, section 15 of Finnish Company Act). A similar, but not identical, duty of information ("deberes de información de la pertenencia al grupo"), complemented by a duty of publicity on commercial registry ("Deber de inscripción del grupo"), was also provided by the 2013 Spanish Proposal of a Code on Commercial Companies (sections 291-7 and 291-8).

According to paragraph 2, in case of establishing control, it is necessary also for the subsidiary to inform the parent company of any shares or voting rights held in other companies, since this can have the effect of extending the scope of the group, by extension to previously existing subsidiaries or by creation of new ones.
thanks to the addition of shares and/or voting rights held by the parent and the new subsidiary.

This duty only applies to national subsidiaries (but also in respect to foreign parent companies), since the law of a State cannot prescribe obligations to foreign companies.
PART 2
GROUP MANAGEMENT

Section 9
Right of a parent company to give instructions to the management of a subsidiary

(1) A parent company has the right to give instructions to the organ of management of their subsidiaries, subject to exceptions in subsections (2) and (3). A subsidiary may receive instructions from the management of a foreign parent company.

(2) Subject to conditions specified in section 16, the organ of management of a subsidiary shall comply with the instructions issued by its parent.

(3) The following members of the management of a subsidiary are not bound by any instruction:

   (a) Directors and managers who were not appointed by the parent company or by the controlling shareholder, especially following the application of the articles of associations, of a shareholders’ agreement or of any law or regulation.

   (b) Directors who are defined as “independent directors” according to the applicable Corporate Governance Code.

   (c) Directors who are employee representatives.

(4) A non wholly-owned subsidiary needs to disclose in the Commercial registry whether or not its management is directed by the parent. Unless a contrary disclosure, a wholly-owned subsidiary is presumed to be subject to instructions of its parent company and does not need to make a disclosure in the Commercial registry, except that it is wholly-owned. This disclosure is for information of third parties and shareholders only.

Comments

As a matter of fact, in groups, subsidiaries receive instructions, whether oral or written, from the management of the parent company. However, in the overwhelming number of Companies Acts, this reality is not recognized due to the predominance of the concept of the legal autonomy of the subsidiary. This provision is designed to reconcile law and the reality by treating subsidiaries in a different way as than autonomous companies.
Some national legal orders (e.g., Germany) recognize a legal power of direction to parent companies only on the condition that a “legal group” is formed, that is, the parent assumes in advance special rights and liabilities toward the subsidiary (e.g., duty to cover annual losses), its creditors (e.g., unlimited liability in the case of wholly-owned subsidiaries in Germany)\(^\text{20}\) or its minority shareholders (e.g., compensation and sell-out rights).

Likewise, the Forum Europaeum had a similar view and proposed that the parent, under certain conditions, be «entitled by unilateral declaration to assume the management of the subsidiary ». However, the regime proposed by Forum Europaeum proposal was subject to certain rules which are not adopted by the EMCA. This approach was similar to the German intercompany agreements (Section 291-307 of the Aktiengesetz or AktG)

The Forum Europaeum proposal conditioned the right to assume management of the company to an « unilateral declaration » which would be « registered in the Commercial Registers of both the parent and subsidiary ». This proposal is not kept as it would be a formal requirement which does not seem necessary, since the EMCA does not create a special liability towards third parties only because instructions are given (see however section 17 on wrongful trading).

However, the EMCA provides that a non wholly-owned subsidiary needs to disclose in the Commercial registry whether or not its management is directed by the parent. This disclosure is for information of third parties and shareholders only. It does not trigger any specific right and is simply a matter of transparency. It is at the discretion of the directors to decide at what point to publish the declaration, taking into account the number of instructions received, their importance, or simply the existence of a group-wide policy.

The Forum Europaeum proposal also conditioned the right to assume management of the company to the holding by the parent of « a sufficient majority to enable it to alter the Articles of Association of a subsidiary ». The EMCA does not adopt such limitation, although as soon as control is established, whatever the level, the management and the board of directors of the subsidiary will normally feel compelled to follow instructions by the parent company. For the same reason, it is not proposed to limit this power to give instruction to wholly-owned companies.

Finally, in the proposal of the Forum Europaeum, « the legal consequence of the Group Declaration include the assumption of the parent of liability for losses in the subsidiary in case of winding-up (creditor-protection) and the obligation to compensate minority shareholders in the subsidiary (minority protection) ».

The approach chosen in EMCA is to consider groups and the power of direction of parent companies over subsidiaries as a reality which has not to be formally “legalized” or “declared”. Why would the parent company form a “legal group”

\(^{20}\) Section 322 German AktG.
with their subsidiaries, if the price for obtaining a legitimation of its power of direction is so high? Why would the parent enter into such a “unilateral declaration”, whereas as a matter of fact, it can already instruct the subsidiary, and face increase risk of liability? However, as a simple matter of information for third party and minority shareholders, non wholly-owned subsidiaries have to indicate in the Commercial registrar and in their annual account whether they are subject to instructions by the parent company. In the case of wholly-owned subsidiaries, they are presumed to be subject to such instructions. The presumption can be reversed by a declaration to the contrary in the Commercial register. The right to give instruction exists regardless of whether the disclosure has been made.

The subsidiary must fulfil the instructions given by the parent company. Otherwise, the managers and directors of the subsidiary shall resign.

Accepting the power of direction of parent companies over subsidiaries as a “de facto” phenomenon, does not mean to accept that it can be exercised without any limits or constraints.

First of all, the right of the parent to issue binding instructions to subsidiaries is limited by the conformity to the interest of the group (section 10 of the chapter). If the instructions are contrary to the interest of the subsidiary and not in conformity with the conditions set in section 10, the organ of management of the subsidiary will be liable for breach of their duty of care.

Secondly, minority shareholders of the subsidiary are sufficiently protected either by the general rules or by sell-out rights, providing them with an exit avenue to the group situation.

Thirdly, creditors and third parties enjoy also a case-by-case protection in case of subsidiary insolvency by the general provision of “wrongful trading” of section 17, in chapter 16).

Finally, some organs of management of a subsidiary are not bound by the instructions. This is the case in subsidiaries where such organs are not appointed by the parent company. The exception covers shareholders’ agreement in case a non-controlling shareholder is entitled to a representation to the board. The reason is that specific protection that minority shareholders have bargained for should not be removed by the fact that the company belongs to a group. These protection should be respected. Although the EMCA recognizes that the situation of listed subsidiary is specific and protection of the public should be set at a higher level, section 9 applies to them. The reason is that there is no logical reason to distinguish between listed and non listed companies, especially provided that there are significant protections in other chapters for minority shareholders (sell-out rights) and creditors (wrongful Trading). However, the rule should not apply to “independent directors”, who are being required by listed companies regulations and Corporate Governance Codes, since it would be
contrary to their independence. The same exception also applies explicitly to “directors who are employee representatives”.

The right to give instructions is vested in the company organ entitled to manage and represent the company according to EMCA. Instructions may have any form (written, oral, etc.) and may only be addressed to the organ of management of the subsidiary.

The right to give instructions benefits any parent company, not just the direct parent company. This will provide flexibility in the organisation of the group, since the ultimate parent company can let another subsidiary, with regional competence for instance, give instructions to sub-subsidiaries.

The right to give instructions benefits any parent company, as to all subsidiaries, including foreign subsidiaries as long as the foreign law allows subsidiaries to receive instructions from a parent company. Similarly, the EMCA provides, in Paragraph (1), that subsidiaries can receive instructions from a foreign parent company.

Section 10
Right of access to information at the level of the subsidiary

The board of directors, or equivalent body, and the management of the parent company, including a foreign one, has the right to obtain the communication of any information from a subsidiary, unless such communication would violate the law of the country whose rules apply to the subsidiary or the rights of third parties.

Comments

Groups need information from the subsidiaries for legal reasons, such as establishing the accounts. Groups who are acting as integrated entities usually also need information from the subsidiaries for business reasons, such as assuring quality control across subsidiaries.

A similar provision exists in some national companies Act (Denmark).

Of course, the right of access to information of the parent company is subject to limits. The reference to the violation of the «the law of the country whose rules apply to the subsidiary» includes different types of rules (e.g. banking secrecy) and different types of companies (national and foreign subsidiaries). Likewise, rights of third parties may not be affected by such right of access to information (e.g. transfer of valuable data, like clients data). Protection could then be organized through the concept of «corporate opportunity» (section 13).
This provision will also facilitate the enforcement of the special investigation mentioned in section 16, since the management of the parent company, when requested by a special examiner, will not be able to argue that it cannot access this information.

This power should be recognized also to a foreign parent company.

**Section 11**

**Right to squeeze-out**

(1) A parent company, controlling more than 90% of the shares and votes of the subsidiary, may demand that the other shareholders have their shares redeemed. In this case, the other shareholders must be requested, under the rules governing notice for general meetings, to transfer their shares to the shareholder within four weeks.

(2) The terms of redemption and the basis used for determining the redemption price must be set out in the request. It must also be stated in connection with the redemption that in the event that no agreement can be reached on the redemption price, such price will be fixed by an expert appointed by the court with jurisdiction over the place where the registered office of the company is situated. The request must include a statement by the central governing body of the controlled company on the general terms of redemption.

**Comments**

The right to squeeze out minority shareholders is recognized in many national laws (section 70 of the Danish Companies Act, section 327a-327f of the German Corporation Act, section 49c of Greek Corporation Law, section 490 of the Portuguese Companies Act). In several others, it is restricted to listed companies (e.g., “offre de retrait obligatoire” in France, “offerta d’acquisto residuale” in Italy, etc.). Section 11 applies to listed and unlisted subsidiaries alike.

The possibility to squeeze-out minority shareholders is the counterpart of the sell-out rights included in the EMCA. It is also a way to facilitate the formation of fully integrated groups.

Also article 15 of the Thirteenth directive on takeovers, under certain conditions, grants any shareholder acquiring 90% (or more, depending on the Member State) of the voting shares of a listed corporation through a tender offer, the right to cash out minorities at a fair price.

The Forum Europaeum also proposed to create a squeeze-out right when a shareholder held 90% or 95% of the shares.
The Danish Companies Act, especially as to the determination of the redemption price, served as model for section 11.

According to EMCA, a company can have a single shareholder (see Chapter 2 Formation of companies).
PART 3
PROTECTION OF SHAREHOLDERS OF THE PARENT COMPANY

Section 12
Right of information and to request a special information

The relations between the companies of the group, including with companies formerly members of the group, are open to the right of information and to the right to request a special investigation, as provided in Chapter 11 (General Meetings and Principles of Minority Protection).

Comments

Most national companies law provide for some sort of investigation right.

This provision, which is linked to the right to ask questions in Chapter 11 (General Meetings and Principles of Minority Protection) aims to prevent management of the parent company to refuse to answer questions about the situation of the group as a whole on the basis that the information would be located at the level of a subsidiary. Similar provisions can be found in some legal orders (e.g., section 32 of Swedish Company Act, section 102 of the Danish Company Act, section 290 of Portuguese Companies Act).

Likewise, whereas the right to request a special investigation is a general right covered in the Chapter on Shareholders’ meeting and minority protection, it is particularly important in groups, especially since the information might be available only at the level of the subsidiary. The Forum Europaeum was of the same view and proposed that the parent, under certain conditions, be « entitled by unilateral declaration to assume the management of the subsidiary». However, the regime proposed by the Forum Europaeum proposal was more restrictive. It required a reasonable suspicion of « gross breach » of the law or of the Articles of Association, and not just a simple breach.
PART 5
PROTECTION OF SHAREHOLDERS AND CREDITORS OF THE SUBSIDIARY

Section 13
Corporate opportunity within a group

When a subsidiary is not wholly-owned, a parent company, including a foreign one, must not itself or through another subsidiary exploit a corporate opportunity unless it has received the approval of the disinterested directors of the subsidiary, and if there are none, of the non-controlling shareholders of the subsidiary.

Comments

A parent company will usually be a director of the subsidiary and, on that capacity, it would be subject to the general prohibition of benefiting from corporate opportunities, unless he has received the approval of the board by the disinterested directors (see EMCA Chapter 9, Directors’ duties). However, a parent company might not always be a director, for instance because it is located several levels above the level of the subsidiary.

In the case of a subsidiary, it is less possible to rely on disinterested directors of the subsidiary.

The prohibition applies to a foreign parent company. It also applies to a national parent company regarding its foreign subsidiaries.

Section 14
Right of shareholders to request a special investigation

The shareholders of a subsidiary can request a special investigation in the parent company, under the same conditions as mentioned in section 12.

Comments

The right of the expert to investigate should also apply upstream. The Forum Europeaum proposal included this point but it was not very specific. This possibility of an upstream special investigation is provided for by Dutch company law (Section 351, al. 2, of the Dutch civil code).
The right of shareholders to request a special investigation into decisions of the parent company is limited to decisions which have affected the subsidiary.

Section 15
Right to sell-out

(1) When a parent company owns directly or indirectly more than 90% of the shares and of the voting rights, the others shareholders may request that their shares be purchased by the parent company.

(2) The shareholders of a subsidiary can request in court that the parent company or another person designated by it purchase their shares.

(3) The terms of redemption and the criteria used for determining the price must be set out in the request. It must also be stated in connection with the redemption that in the event that no agreement can be reached on the redemption price, such price will be fixed by an expert appointed by the court with jurisdiction over the place where the registered office of the company is situated.

(4) This provision does not apply in a foreign subsidiary.

Comments

The provision in paragraph (1) is the equivalent to the squeeze-out right of section 11. A similar provision is recognized today by national laws, like Poland (“reversed squeeze-out” of section 4181 of the Portuguese Company Act), Portugal (“right to be bought” of section 490, nº 5 and 6 of Portuguese Company Act) or Hungary (Section 3: 53(1) and 3 : 324(2) of the new Hungarian Civil code, applicable starting as of 15 March 2014). In several other Member States the sell-out right is restricted to listed companies (e.g., France).

A very interesting regime on sell-out rights is to be found in the part on groups of the Italian Civil code, which was introduced in 2003.21 The Italian regime served as a model for section 15, but with some differences since less in the EMCA situations give rise to a right to sell-out. On the one hand, the EMCA was mindful not to create a situation were the ease of exercising the right of withdrawal would force groups to maintain an higher level of cash than would be necessary for business purposes. On the other hand, the EMCA does not subject the exercise of sell-out rights to the fact that the parent company exercises direction to the subsidiary.

21 Art. 2497-quater of the Italian Civil code. See Paola FASCIANI, Groups of companies: The Italian approach, ECFR 2007, at. 228.
The provision in paragraph (2) allows shareholders who consider that they are victim of an abuse by majority shareholders to file a petition in court requesting their shares to be bought back. The provision does not refer to the German concept of an "important cause" (Wichtiger Grund), which leaves a significant freedom to judges to decide. In addition to an abuse of majority, such cases could be, for instance, unfair prejudice, the lack of payment of dividends for a long period, the existence of detrimental related party transactions, etc.

**Section 16**

**Interest of the group**

(1) If the management of a subsidiary, especially as a result of an instruction issued by the parent company, takes a decision which is contrary to the interests of its own company, it shall not be deemed to have acted in breach of their fiduciary duties if:

(a) the decision is in the interest of the group as a whole, and

(b) the management may reasonably assume that the loss/damage/disadvantage will, within a reasonable period, be balanced by benefit/gain/advantage and,

(c) the loss/damage/disadvantage, referred to in the first sentence hereof, does not include any which would place the continued existence of the company in jeopardy.

(2) If the subsidiary is wholly-owned, paragraph (1)(b) does not apply.

(3) The management of the subsidiary may refuse to comply with instructions from the parent company in case the conditions set in paragraph (1) are not satisfied.

**Comments**

Section 16 is a complement to Section 9 (Right of a parent company to give instructions to the management of a subsidiary) and recognizes the notion of the “interest of the group”. It creates a basic rule, in compliance with which directors and managers of a company, member of a group, may either exercise or be subject to a directing and coordinating activity.

The recognition of the interest of the group would be helpful not only for the parent company but also for the directors of the subsidiary company. As mentioned in the Report of the Reflection Group On the Future of EU Company Law (2011) "A major advantage of the recognition of the interest of the group is that it provides more clarity to the directors of the subsidiary as to which
transaction or operations they can approve.\textsuperscript{22} The recognition of the interest of the group provides, to a certain extent, this legal certainty.

Section 16 does not provide a definition of the “interest of the group”. The reason is that a satisfactory definition would be very difficult, if not impossible, to find given the almost infinite diversities of situations in groups. Therefore, it is left to judges to decide on a case by case basis. This approach creates some uncertainty but which should be rather limited because judges usually do not tend to second guess the business decisions of management, as long as the company has not filed for bankruptcy.

In general, the lack of definition should act as a supplementary protection for minority shareholders or for creditors alike by allowing judges to apply section 16 in a flexible way.

The approach of the EMCA is similar to the one adopted by most if not all national companies Acts for an individual company. The notion of “social interest” of a company is usually not defined for the same reasons as it should not be defined for a group.

Because of the lack of definition, there is no requirement that the interest of the group should tend towards an harmonisation of the interest of the parent company and the subsidiary. However, in certain circumstances, a judge applying section 16 could adopt this approach.

The approach is influenced by the \textit{Rozenblum} case, which is a criminal case law in France\textsuperscript{23}. In France, the main criminal law tool against self-dealing is the provision against abuse of corporate assets (\textit{abus de biens sociaux}). It punishes, among others, board chairmen, directors or managing directors of a public limited company or a limited liability company who "use the company's property or credit, in bad faith, in a way which they know is contrary to the interests of the company, for personal purposes or to favour another company or undertaking in which they have a direct or indirect interest". The penalty is a prison term of up to five years (with no minimum). French courts have created a special safe harbour in case of abuse of corporate assets within groups (the so-called "\textit{Rozenblum doctrine}"). This doctrine admits a "group defense" under certain conditions. First, there must be a group characterized by capital links between the companies. Second, there must be strong, effective business integration among the companies within the group. Third, the financial support from one company to another company must have an economic quid pro quo


and may not break the balance of mutual commitments between the concerned companies. Fourth, the support from the company must not exceed its possibilities. In other words, it should not create a risk of bankruptcy for the company. This approach is also adopted in the German criminal code.\(^{24}\)

Section 16 is inspired by the Rozenblum doctrine but with some simplifications. The Rozenblum doctrine is sometimes considered, in and outside France, to be obscure and its successful application hardly predictable due to the number of conditions to be satisfied. Therefore, Section 16 adopts a simpler and more flexible approach. The main difference is that there is no requirement that the group has a balanced and firmly established structure. However, the existence of an interest of the group implies that there must be a long-term and coherent group policy.

The Forum Europaeum also adopted the Rozenblum approach but with some modifications. The Forum Europaeum proposal conditioned this protection to the fact that evidence of compliance would « be recorded in a continuous manner » and that the management would report the invocation of the provisions « to the next general meeting of the subsidiary ». This approach is not kept in the EMCA, since it would be formalistic.

Many European countries have similar approaches to the French "Rozenblum doctrine". This is the case in the Nordic countries, in Belgium, in the Netherlands ("Nimox doctrine"), in Italy ("teoria dei vantaggi compensative".\(^{25}\)). The Czech republic recently moved toward a regime similar to Rozenblum.\(^{26}\)

In the UK, directors are able to take into account of the interests of the group in reaching a decision about what will promote the company’s success for the benefit of its members. If there is a doubt that something is in the interests of the company (e.g. giving a guarantee for the benefit of the group), any doubt about whether this involves a breach of the director’s duties can be dealt with by the shareholders passing a resolution to approve the action proposed. However, because directors may incur personal liability for wrongful trading by the company if the company goes into insolvent liquidation and the director knew or ought to have concluded that there was no reasonable prospect of avoiding this and did not take every step to minimize the potential loss to the creditors, directors will be very careful not to prefer the interests of the group over the interests of the creditors of the company if the company may become insolvent.

Section 16(1) protects the managers of the subsidiary against liability, if they take a decision or apply an instruction contrary to the interests of the subsidiary even by taking into account the existence of the group.

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\(^{24}\) Section 266 German criminal code (Strafgezetzbuch).

\(^{25}\) Section 2497 Italian Codice Civile.

\(^{26}\) Section 71 ff, of Czech Law No. 90/2012 on commercial companies and cooperatives (Business Corporations Act). The new Czech Business Corporations Act is applicable as of 1st January 2014.
However, in case an instruction violates section 16(1), the issue must be addressed of whether subsidiary managers “must” obey or “may” refuse to obey?

On the one hand, if the management of the subsidiary “must” obey, it is a relief for the directors as they would be exempted from liability in such case. It also makes the functioning of the group more effective as instructions are always binding. On the other hand, there are severe drawbacks to this approach. First, it would imply a lower level of protection for creditors and minority shareholders, since the directors would not act as a shield in a case where they think that the instructions violates the interest of the subsidiary, even taking into account the interest of the group. This would leave the management of the subsidiary with the only choice to comply or to resign. Both alternatives are not favourable to the minority shareholders, at the very moment where they most need protection. Second, if the parent is located in another Member State or in a foreign State, it might be difficult, complex and costly, for the minority shareholders to sue them in this other State, since the management of the subsidiary will be exempted from liability because the instruction was binding for them. This increases the risk of abuses by parent companies. Finally, even if the recognition of the interest of the group is a necessary and useful relaxation from the protection of the interest of the minority shareholders and of creditors at the level of the subsidiary, this recognition is not without risks. These risks should be mitigated by a cautious approach and any instruction must be given in respect of the law.

From the perspective of an effective management of the group, this approach presents the drawback to allow the directors of the subsidiary, in certain circumstances, to block the power of direction of the parent company. However, such situations where the subsidiary would refuse to execute a binding instruction from the parent company should also remain exceptional. In case the directors refuse to execute but do not resign, the issue could be settled swiftly by the removal of the concerned directors at the next general shareholders’ meeting, possibly following a judicial request of the parent company (See. Chapter 11 General Meetings and Principles of Minority Protection). Therefore, the parent will always have the last word. The opposition by the management of the subsidiary could also lead the parent company to reconsider its decision, possibly after a discussion with the management of the subsidiary or because of complaints by minority shareholders. The interests of the minority shareholders and creditors are better protected by this right to refuse to apply the instruction. The EMCA noted that under German Company law, in the case of a contractual group (Vertragskonzern, Section 302 AktG), the managers of the subsidiary “may” refuse to comply with instructions from the parent company in case of manifest («offensichtlich») violation of the interests of the parent company or of the companies affiliated with it (Section 308(2) AktG).

Therefore, the EMCA has decided that, if an instruction of the parent company violates section 16(1), the management of the subsidiary is not obliged to
comply. The approach of the EMCA seems to be more protective than the German approach since the right to refuse to apply an instruction is granted to the management even if the instruction is not a manifest («offensichtlich») violation of the interests of the parent company or of the companies affiliated with it. However, this is justified since the EMCA approach is more flexible and does not require an automatic compensation of disadvantages.

In case that the management of the subsidiary decides to apply an instruction which violates section 16(1), they will remain liable.

The safe-harbour also applies to wholly-owned subsidiaries. However, in such case, Section 16(2) eliminates the requirement provided for in paragraph (b) that "the management may reasonably assume that the loss/damage/disadvantage will, within a reasonable period, be balanced by benefit/gain/advantage." This is so because if the subsidiary is wholly-owned, the management of the parent and the subsidiary should have more freedom to manage the company and to transfer value as long as they do not place the continued existence of the company in jeopardy.

Section 17
Wrongful trading

(1) Whenever a subsidiary company, which has been managed according to instructions issued by its parent in the interest of the group, has no reasonable prospect of, by means of its own resources, avoiding a winding-up (crisis point), the parent company is obliged without delay to effect a fundamental restructuring of the subsidiary or to initiate its winding-up procedure.

(2) If the parent acts in contravention of paragraph 1 or if it has managed the subsidiary to the detriment of the subsidiary, it shall be held liable for any unpaid debts of the subsidiary company incurred before the crisis point. In such case, it will be presumed that the parent knew or should have known that the subsidiary company had arrived at a crisis point. The court may assess the extent of the creditors' relevant debts.

(3) The right to claim compensation provided for in paragraph 2 hereof can be invoked only by the liquidator/administrator/administrative receiver/receiver of the subsidiary. The insolvency court may itself initiate the said claim.

Comments

Section 17 is close to the concept of "Wrongful trading" which originates in the UK (Section 214 Insolvency Act 1986).
Section 17 is close to the Forum Europaeum proposal but with some modifications. It is also influenced by the Report of the Reflection Group On the Future of EU Company Law (2011) suggested that the "Rozenblum doctrine", if applied at the European level, should distinguish two situations: “(i) where the subsidiary is not close to insolvency and (ii) where it is close to insolvency. In case the subsidiary has no reasonable prospect of, by means of its own resources, avoiding a winding-up (crisis point), directors of the subsidiary should protect creditors and therefore unbalanced transactions to the prejudice of the subsidiary should not be protected”. This is in effect the result reached by Section 17. In case, a subsidiary reaches a crisis point, the parent company has the duty to start without delay insolvency proceedings of the subsidiary, in order to effect a fundamental restructuring or alternatively to liquidate the subsidiary

Section 17 is more restrictive than Section 214 of the UK Insolvency Act and establishes a link between the insolvency of the subsidiary and the instructions given by the parent company.

The formulation ensures the existence of a link between power and liability of the parent company in case of bankruptcy of a subsidiary. As a matter of fact, the default of a subsidiary may be caused by the control exercised by the parent company but may also emerge from purely fortuitous and unpredictable circumstances (e.g., natural catastrophes, strikes, financial crisis, insolvency of important subsidiary debtors, abrupt modification of market environment or legal environment). In such a case, to impute a special liability on parent corporation would be a too rigid solution, creating a windfall protection for subsidiary creditors (which the creditors of independent companies do not enjoy at all) and some input for the adoption of centralized structures of governance of groups (as a way to prevent the event of subsidiary default). By limiting the parent company duties in the event of bankruptcy of the subsidiary (restructuring or winding-up) to the case of those subsidiary which were consistently managed in the interest of the group, and not of its own interest, one could ensure a flexible system of imputation of such duties.

The Forum Europaeum proposal conditioned this protection to the fact that evidence of compliance would « be recorded in a continuous manner » and that the management would report the invocation of the provisions « to the next general meeting of the subsidiary ». This approach is not kept in Section 17, since it would be formalistic.