

FREEDOM OF ESTABLISHMENT OF LEGAL
PERSONS WITHIN THE EUROPEAN UNION:
AN ANALYSIS OF THE EUROPEAN COURT
OF JUSTICE DECISION IN THE
ÜBERSEERING CASE

NICOLE ROTHE*

TABLE OF CONTENTS

| | |
|--|------|
| Introduction..... | 1104 |
| I. Background | 1107 |
| A. Facts and Procedural History of the <i>Überseering</i> Case..... | 1107 |
| B. Real Seat Doctrine vs. Incorporation Theory. | 1110 |
| C. The German Seat Theory Prior to <i>Überseering</i> | 1113 |
| D. European Union Law Regarding Freedom of Establishment. | 1116 |
| II. The Court's Decision in the <i>Überseering</i> Case | 1119 |
| A. The German Courts' Rulings..... | 1119 |
| 1. The German courts' analysis conformed to then- existing German law | 1119 |
| 2. The German courts' analysis conformed to ECJ precedent..... | 1120 |
| B. The ECJ's Judgment..... | 1123 |
| 1. The Treaty provisions on freedom of establishment apply | 1124 |
| 2. A restriction on the freedom of establishment occurred | 1127 |
| 3. The restriction on the freedom of establishment was not justified..... | 1128 |
| 4. Assessment of the ECJ's overall holding..... | 1132 |

* J.D. Candidate, May 2005, *American University, Washington College of Law*, B.A., 2001, *Bennington College*. I would like to thank Professor J.A.E. Vervaele for his guidance and comments on early drafts of the paper, Albena Petrova for alerting me to the *Überseering* decision, Liz Abraham for her editorial suggestions, and the editors and staff of the *American University Law Review* for reviewing the piece and making final edits. A special thanks to Ryan Barolet-Fogarty for his encouragement, patience, and support throughout the process.

| | |
|---|------|
| III. Impact of the <i>Überseering</i> Case | 1134 |
| IV. Recommendations..... | 1137 |
| A. EU Member States Should Amend Their Laws to Comply with the ECJ Ruling | 1137 |
| B. The ECJ Ruling in <i>Überseering</i> Should Be Interpreted Narrowly..... | 1138 |
| C. Even Under a Broad Interpretation, Host States May Require Compliance with Their Regulatory Practices ... | 1139 |
| D. The European Union Should Strive Towards Legal Harmonization to Diminish Conflict-of-Laws Problems | 1140 |
| Conclusion | 1141 |

INTRODUCTION

The European Court of Justice's ("ECJ" and "Court")¹ landmark ruling in *Überseering BV v. Nordic Construction Company Baumanagement GmbH* ("*Überseering*")² raises questions about the validity of corporate conflict-of-laws rules in many European Union ("EU") Member States. The decision grants EU businesses greater freedom of movement within the European Union³ and significantly alters German international company law.⁴ German courts must now recognize "cheap" limited liability companies—entities that were incorporated under the looser regulations of another EU Member State.⁵ This development casts doubt on the continued utility of the real seat doctrine⁶ as a conflict-of-laws principle.⁷ At stake is the

1. This Note refers to the European Court of Justice as both "ECJ" and the "Court."

2. Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002).

3. See discussion *infra* Part III (suggesting that the Court's requirement that host states afford companies legal recognition enables companies to move more easily across borders within the European Union).

4. See discussion *infra* Part II.B.4 (observing that the ECJ rejected Germany's strict requirement that a foreign-incorporated entity reincorporate in Germany upon transferring its seat to Germany).

5. See Maximilian Steinbeis, *EuGH erzwingt Öffnung für "Billig-GmbHs,"* HANDELSBLATT, Nov. 6, 2002 (commenting that the ECJ's *Überseering* ruling enables promoters of an entity to circumvent German company formation laws by incorporating under less stringent restrictions in countries such as Great Britain or the Netherlands). The minimum capital requirements for the formation of a company in Great Britain are substantially lower than those in Germany. *Id.* To ensure the protection of creditors, promoters must furnish at least € 25,000 to form a company in Germany, whereas Great Britain requires only £100 for the formation of a similar limited liability company. *Id.*

6. This Note uses the terms "real seat doctrine," "seat theory," and "company seat principle" interchangeably.

7. See discussion *infra* Part III (stating that the ECJ's *Überseering* ruling could be construed as abolishing the real seat doctrine but arguing that the decision should

ability of a host country to impose its legal, economic, and social values on companies based within its borders but incorporated elsewhere. For example, without the real seat doctrine, Germany may no longer be able to enforce its higher minimum capital requirements and protection of workers' participation in management because companies could simply circumvent these rules by incorporating in a country with less stringent standards.⁸ This Note advocates a narrow interpretation of the *Überseering* ruling, which modifies, but does not abolish, the seat theory.

In its decision, the ECJ held that when a company incorporated in one EU Member State moves its central place of management to another Member State, the host country must recognize the entity and allow it access to the host country's courts.⁹ In *Überseering*, a company incorporated in the Netherlands moved its center of administration to Germany and sought to enforce its contractual rights against a German company before German courts.¹⁰ The German courts applied the German version of the real seat doctrine and dismissed the suit, noting that the Dutch company did not have legal capacity in Germany because the entity was incorporated in one state but had its seat in another state.¹¹ The ECJ decided that a host state's denial of legal capacity to a foreign entity with its place of administration in the host state violates the freedom of establishment guaranteed under the Treaty Establishing the European Community ("EC Treaty").¹²

be interpreted narrowly as merely modifying the seat theory). *See generally infra* notes 43-48 and accompanying text (defining the real seat doctrine and incorporation theory as the two principal approaches for determining a corporation's nationality—that is, the country whose law will govern the company when it has contacts with more than one jurisdiction).

8. *See infra* note 73 and accompanying text (providing examples of unique company law standards in Germany that companies could avoid if the incorporation theory became the governing conflict-of-laws principle).

9. *See* Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶¶ 94-95 (rejecting Germany's strict requirement of reincorporation as inconsistent with the Treaty provisions on freedom of establishment), available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002). The transfer of a company's place of administration constitutes the formation of a primary establishment. *See, e.g., id.* ¶¶ 42-43. This is different from the formation of a branch—a secondary establishment. *See, e.g., id.*

10. *See id.* ¶¶ 2, 6, 8 (noting that the contractual dispute arose between the Dutch company, *Überseering BV*, and the German entity, *Nordic Construction Company Baumanagement GmbH*, when *Überseering BV* alleged that *Nordic Construction* performed its contractual obligations inadequately).

11. *See id.* ¶¶ 9-10 (outlining the procedural history of the *Überseering* case).

12. *Id.* ¶¶ 94-95; CONSOLIDATED VERSION OF THE TREATY ESTABLISHING THE EUROPEAN COMMUNITY, arts. 43-48, Dec. 24, 2002, O.J. (C 325) 1 (2002) [hereinafter EC TREATY] (enshrining the freedom of establishment).

This Note analyzes the ECJ's decision in *Überseering*. Part I introduces the facts and procedural history of the case and compares the real seat doctrine and the state-of-incorporation theory.¹³ Part I also discusses Germany's strict interpretation of the seat theory and details applicable EU law.¹⁴ Part II examines the German courts' application of the real seat doctrine to *Überseering* BV.¹⁵ In addition, Part II analyzes the ECJ's findings regarding three questions: whether the Treaty provisions on freedom of establishment applied to the *Überseering* case;¹⁶ whether the application of the German seat theory had resulted in a restriction of the right of establishment;¹⁷ and whether a justification existed for that restriction.¹⁸ Part II concludes with an assessment of the ECJ's overall holding in *Überseering*.¹⁹

Part III evaluates the impact of the case. It argues that the decision should be interpreted narrowly as modifying the real seat doctrine to ensure that host states afford legal recognition to foreign-incorporated entities, so as to allow them access to the host state's courts.²⁰ Part III rejects the broad interpretation that the ECJ's ruling

13. See discussion *infra* Parts I.A, I.B (detailing the origin and procedural history of the *Überseering* action and juxtaposing the seat and incorporation theories as alternative approaches to conflict-of-laws problems concerning companies incorporated in one EU Member State and having their place of management in another Member State). This Note uses the terms "incorporation theory/doctrine," and "state-of-incorporation theory/doctrine" interchangeably.

14. See discussion *infra* Parts I.C, I.D (noting that foreign-incorporated entities with their seat of management in Germany could be denied legal capacity under the German real seat doctrine and discussing the Treaty provisions on the freedom of establishment).

15. See discussion *infra* Part II.A (suggesting that the German courts' analysis in the *Überseering* case was correct under then-existing German and EU law).

16. See discussion *infra* Part II.B.1 (reporting that the ECJ found that the Treaty's right of establishment provisions applied to a company such as *Überseering* BV, which was incorporated in one Member State and moved its center of administration to another Member State).

17. See discussion *infra* Part II.B.2 (agreeing with the ECJ that Germany's denial of *Überseering* BV's legal capacity and access to courts, which resulted from the German reincorporation requirement, constituted a restriction of the freedom of establishment).

18. See discussion *infra* Part II.B.3 (examining the ECJ's finding that the denial of a foreign company's legal capacity is excessive). Part II.B.3 also analyzes the Court's discussion of possible justifications for a restriction on the freedom of establishment when the restrictive measures do not amount to an outright negation of the freedom. *Id.*

19. See discussion *infra* Part II.B.4 (suggesting that the ECJ intentionally avoided choosing between the real seat doctrine and state-of-incorporation theory by limiting the scope of its judgment). The ECJ limited its holding to the requirement that host states recognize the legal capacity of companies that have their seat in the host state but are incorporated elsewhere. *Id.* Part II.B.4 also suggests that the Court should have clarified exactly what type of compelling public interest considerations would sufficiently justify a restriction on the right of establishment. *Id.*

20. See discussion *infra* Part III (noting that the ECJ did not discuss which

abolishes the real seat doctrine and adopts the incorporation theory.²¹

Part IV recommends four ways of addressing the *Überseering* ruling. First, EU Member States should review and amend their national laws to comply with the ECJ's decision.²² Germany, in particular, should replace its strict requirement of reincorporation with other means of regulatory enforcement.²³ Second, *Überseering* should be interpreted narrowly as modifying, but not abolishing, the real seat doctrine.²⁴ In the alternative, host states should be able to force foreign companies to comply with local regulatory protections.²⁵ Finally, Part IV suggests that EU Member States should strive towards legal harmonization in order to diminish the significance of the distinction between the real seat doctrine and state-of-incorporation theory and resulting conflict-of-laws problems.²⁶

I. BACKGROUND

A. *Facts and Procedural History of the Überseering Case*

The ECJ decision in *Überseering* arose out of a contractual dispute between a German corporation, Nordic Construction Company Baumanagement GmbH ("Nordic Construction"), and a Dutch company, *Überseering BV*.²⁷ Nordic Construction was incorporated

conflict-of-laws principle should govern EU company law and limited its ruling to rejecting Germany's strict requirement of reincorporation).

21. See discussion *infra* Part III (arguing that the *Überseering* decision does not permit such a broad interpretation because the ECJ did not discuss which state's laws should apply to the company beyond the host state's initial recognition of the company's legal capacity).

22. See discussion *infra* Part IV.A (suggesting that EU Member States modify their international company laws to ensure legal recognition of companies that are incorporated in a different EU Member State but have their seat in the host country).

23. See discussion *infra* Part IV.A (suggesting that Germany comply with the ECJ ruling in *Überseering* by eliminating the requirement of reincorporation that it imposed on foreign companies that had moved their place of management to Germany and later sought to bring legal proceedings there).

24. See discussion *infra* Parts IV.B, IV.C (arguing that a narrow interpretation, or at least a limitation on the broad interpretation, is necessary to prevent the race to the bottom that would result from enabling companies to circumvent national regulations by incorporating abroad).

25. See discussion *infra* Parts IV.B, IV.C.

26. See discussion *infra* Part IV.D (noting that the only means of resolving the conflict between the real seat doctrine and state-of-incorporation theory as alternative approaches to conflict-of-laws problems is to harmonize company laws in the European Union).

27. See Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶¶ 6-12 (reciting the facts and procedural history of the case), available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002); Judgment of

in Germany,²⁸ while Überseering BV was incorporated in the Netherlands.²⁹ In 1992, Überseering BV hired Nordic Construction to renovate a garage and motel on a piece of land it owned in Düsseldorf, Germany.³⁰ In 1994, two German nationals purchased all shares of Überseering BV.³¹ After Nordic Construction completed its obligations under the project-management contract, Überseering BV accused it of defective contract performance.³²

Überseering BV obtained no compensation from Nordic Construction for the defective work and filed an action for contract damages before a German Regional Court (“lower court”) in 1996.³³ The lower court dismissed the complaint as inadmissible, a decision which the Higher Regional Court affirmed in September of 1998.³⁴

March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶¶ 21-29 (outlining the legal dispute underlying the *Überseering* case); see also Werner F. Ebke, *The “Real Seal” Doctrine in the Conflict of Corporate Laws*, 36 INT’L LAW. 1015, 1026 (2002) (describing the origins of the *Überseering* matter).

28. *Überseering*, 2002 E.C.R. ¶ 2.

29. *Id.* (observing that Überseering BV was registered in Amsterdam and Haarlem on August 22, 1990); see Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶¶ 21, 24 (noting that Überseering BV is a *Besloten Vennootschap met beperkte aansprakelijkheid*, or limited liability company, under Netherlands law).

30. *Überseering*, 2002 E.C.R. ¶ 6 (explaining that Überseering BV employed Nordic Construction to refurbish the two buildings according to a project-management contract between Überseering BV and Nordic Construction, dated November 27, 1992).

31. See *id.* ¶¶ 7, 9 (recounting that two Germans from Düsseldorf purchased the shares in December 1994).

32. See *id.* ¶ 6 (relaying that Überseering BV asserted that Nordic Construction’s paint work was flawed).

33. See *id.* ¶¶ 6, 8 (stating that Überseering BV sued Nordic Construction before the *Landgericht*, or Regional Court, of Düsseldorf, Germany); Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶ 25 (explaining that in its claim, Überseering BV sought the payment of 1,163,657.77 DM plus interest for the correction of the defective work and resulting damages).

34. See *Überseering*, 2002 E.C.R. ¶¶ 9-10 (explaining that Überseering BV appealed to the *Oberlandesgericht*, or Higher Regional Court, of Düsseldorf, Germany, upon dismissal of the action in the Regional Court). See generally FRITZ BAUR & GERHARD WALTER, *EINFÜHRUNG IN DAS RECHT DER BUNDESREPUBLIK DEUTSCHLAND* (6th ed. 1992); LIBRARY OF CONGRESS COUNTRY STUDIES, *GERMANY: A COUNTRY STUDY: THE JUDICIARY*, at [\(http://memory.loc.gov/cgi-bin/query/r?frd/cstdy:@field\(DOCID+de0127\)\)](http://memory.loc.gov/cgi-bin/query/r?frd/cstdy:@field(DOCID+de0127)) (Aug. 1995) (on file with the American University Law Review) (giving an introduction into the German legal system). The German court system contains four levels. *Id.* *Amtsgerichte*, or local courts, constitute the first level and hear minor criminal or civil cases. *Id.* On the next level are the over 100 *Landesgerichte*, or regional courts, which have original jurisdiction over most civil and criminal matters and review appeals from local courts. *Id.* Above these are the *Oberlandesgerichte*, or higher regional courts, which review points of law raised in lower courts and have original jurisdiction over constitutional cases or those involving treason. *Id.* These courts are also the highest authority on the minor cases introduced in the local courts. *Id.* The court of highest appeal for most cases is the *Bundesgerichtshof*, or Federal Court of Justice, which has no original jurisdiction. *Id.* Additionally,

Both courts determined that *Überseering* BV lacked legal capacity in Germany as a company incorporated in the Netherlands with its center of administration in Germany.³⁵ *Überseering* BV then appealed to the Federal Court of Justice,³⁶ which stayed the proceedings and certified questions to the ECJ for a preliminary ruling in March 2000.³⁷ Specifically, the Federal Court of Justice sought guidance on whether a finding of no legal capacity would be inconsistent with the freedom of establishment guaranteed under the EC Treaty.³⁸

The ECJ issued its ruling in the *Überseering* case on November 5, 2002.³⁹ The Court held that Germany had to recognize the legal capacity of *Überseering* BV in accordance with the freedom of establishment guaranteed under the EC Treaty.⁴⁰ The Court concluded that a host state's denial of a company's legal capacity is incompatible with the freedom of establishment, and the Court required host states to recognize foreign-incorporated entities.⁴¹ Based on this preliminary ruling by the ECJ, the German Federal Court of Justice reversed the judgment of the Higher Regional Court and remanded the case for a ruling consistent with the ECJ's interpretation of the Treaty provisions on the freedom of establishment.⁴²

Germany maintains separate specialty courts for administrative, labor, social, fiscal, and patent law, each with their own appeal structure. *Id.* Lastly, the German Federal Constitutional Court hears appeals regarding the rights guaranteed under the Constitution ("Basic Law") or disputes between branches of government. *Id.*

35. Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶ 28; *see Überseering*, 2002 E.C.R. ¶ 9 (explaining that the finding of no legal capacity precluded *Überseering* BV from filing legal actions in Germany).

36. Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶ 29; *Überseering*, 2002 E.C.R. ¶ 11; *see Ebke*, *supra* note 27, at 1022 (remarking that the Federal Court of Justice, or *Bundesgerichtshof*, is the highest court for civil actions in Germany).

37. Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶¶ 13-18; *Überseering*, 2002 E.C.R. ¶ 21. While the appeal was pending in the Federal Court of Justice, *Überseering* BV was sued in a different German court and ordered to pay architects' fees for the property it owned in Düsseldorf, Germany. *Id.* ¶ 12.

38. *See* Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶¶ 15-18; *Überseering*, 2002 E.C.R. ¶ 21.

39. *See Überseering*, 2002 E.C.R. ¶ 94 (holding that a host state's denial of legal capacity to a company incorporated in one Member State and having its seat in the host state violates the freedom of establishment enshrined in the EC Treaty).

40. *See id.* ¶¶ 94-95 (declaring that host states may not refuse to recognize a foreign corporation's legal capacity and may not deny it access to the national courts when the company moves its seat to the host country).

41. *Id.*

42. *See* Judgment of March 13, 2003, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718.

B. *Real Seat Doctrine vs. Incorporation Theory*

The real seat doctrine and the incorporation theory are two competing approaches to determining which state's laws will govern a company's internal affairs when it has contacts with more than one jurisdiction.⁴³ This determination of a corporation's "nationality" becomes relevant when corporate conflict-of-laws problems arise, particularly in the European Union, where significant differences exist in the substantive laws of the Member States.⁴⁴ Under the seat theory, the controlling law will be that of the country where the company's headquarters are located.⁴⁵ By contrast, the incorporation theory requires the use of the law of the incorporation state.⁴⁶ Many EU Member States, including Germany,⁴⁷ France, Italy, and Spain, adhere to the real seat doctrine, while the Netherlands, Great Britain, Ireland, and Denmark follow the incorporation theory.⁴⁸

43. See Christian Kersting, *Corporate Choice of Law: A Comparison of the United States and European Systems and a Proposal for a European Directive*, 28 BROOK. J. INT'L L. 1, 37 (2002) (remarking that the real seat doctrine and state-of-incorporation theory constitute the "two principal competing theories" regarding the determination of corporate nationality); see also Lan Cao, *Corporate and Product Identity in the Postnational Economy: Rethinking U.S. Trade Laws*, 90 CAL. L. REV. 401, 450-51 (2002) (proposing the domestic participation test as an alternative means of determining corporate nationality that is better suited for the "postnational" economy). The domestic participation test grants nationality to a corporation if its business constitutes a "substantial, socioeconomic participation in the state's economy." *Id.* at 454. If the firm meets those requirements, then it will be deemed a domestic company—regardless of where it has its place of incorporation or its seat. *Id.*

44. See *infra* notes 209-10 and accompanying text (discussing some of the major differences between the corporate laws of the EU Member States, particularly German and British rules on company formation).

45. See *infra* notes 50-57 and accompanying text.

46. See *infra* notes 58-62 and accompanying text.

47. See Ebke, *supra* note 27, at 1022-23 (stating that the German Federal Court of Justice adopted the real seat doctrine as the governing conflict-of-laws principle after World War II; all German courts have consistently applied it since).

48. See Kersting, *supra* note 43, at 2 (observing that many EU Member States endorse the company seat principle); see also Ebke, *supra* note 27, at 1016 (claiming that the majority of countries in the European Union follow some form of the seat theory); Danny Ray Garza, *Which Style Should Govern?*, 11 CURRENTS: INT'L TRADE L.J. 76, 78 (2002) (remarking that a number of EU Member States adhere to the company seat principle); Klaus Heine, *Regulatory Competition Between Company Laws in the European Union: The Überseering Case*, 38 INTERECONOMICS 102 (2003) (noting that Germany, France, Italy, and Spain have incorporated the real seat doctrine into their laws); Catherine Holst, Note, *European Company Law After Centros: Is the EU on the Road to Delaware?*, 8 COLUM. J. EUR. L. 323, 323 (2002) (reporting that the Netherlands, the United Kingdom, Ireland, and Denmark follow the state-of-incorporation theory, while the remaining EU Member States adhere to the real seat doctrine) (citing Robert R. Drury, *The Regulation and Recognition of Foreign Corporations: Responses to the "Delaware Syndrome,"* 57 CAMBRIDGE L.J. 165, 187 (1988)). See generally Katharina Pistor et al., *The Evolution of Corporate Law: A Cross-Country Comparison*, 23 U. PA. J. INT'L ECON. L. 791, 865-66 (2002) (outlining the historical origins of the real seat doctrine); Jens C. Dammann, Note, *The Future of Codetermination After Centros: Will German Corporate Law Move Closer to the U.S. Model?*,

The ECJ ruling in the *Überseering* case addressed the German courts' application of the real seat doctrine to *Überseering BV*, which had resulted in a denial of the company's legal capacity and the ability to bring legal proceedings in Germany.⁴⁹ Under the seat theory, only the law of the state with the most significant relationship to the corporation should govern its internal affairs,⁵⁰ including its "formation, its life, and its liquidation."⁵¹ Accordingly, only the country where the company has its seat may regulate it because the company's activities affect that state the most.⁵² A corporation's "seat" is its place of management—its real or effective seat, rather than the seat that is memorialized in the company's articles of incorporation.⁵³

The principle underlying the seat theory is a desire to impose the host state's company law standards.⁵⁴ The theory is based on the conviction that a company should abide by the laws of the state where it carries on its principal business and should not be able to escape the "legal, economic, and social values" of that country.⁵⁵ The real

8 FORDHAM J. CORP. & FIN. L. 607, 609, 610-11 (2003) (noting that EU Member States have traditionally followed the real seat doctrine, while the United States has adopted the state-of-incorporation theory) (citing RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 302(2) (1971)).

49. See *Überseering* 2002 E.C.R. ¶¶ 2, 9-11, 21 (2002) (describing the proceedings that led the German Federal Court of Justice to refer the case to the ECJ for a preliminary ruling).

50. See Ebke, *supra* note 27, at 1015 (commenting that the seat theory is a conflict-of-laws principle that is based on the assumption that only the law of one country should regulate the internal affairs of a company). According to the real seat doctrine, the most appropriate country to regulate a corporation is the country where the company has its headquarters, or the country with which the company has the most significant commercial ties. *Id.* at 1015-16.

51. *Id.* at 1023; see Garza, *supra* note 48, at 78 (noting that the term "internal affairs" contains, among other things, the relations between a company's shareholders, officers, and directors) (citing Werner F. Ebke, *Company Law and the European Union: Centralized Versus Decentralized Lawmaking*, 31 INT'L LAW. 961, 967 (1997)).

52. See Ebke, *supra* note 27, at 1027 (claiming that the seat theory assumes that the real seat country is most affected by a company's actions).

53. See *id.* at 1016 (explaining that the real seat of a company is generally its place of management). According to the interpretation of the German Federal Court of Justice, the real seat of a company is "where 'the fundamental business decisions by the managers are being implemented effectively into day-to-day business activities.'" *Id.* at 1022 (quoting Judgment of March 21, 1986, Bundesgerichtshof (German Federal Court of Justice) BGHZ 97, 269 (272)).

54. Ebke, *supra* note 27, at 1027-28.

55. *Id.* at 1028. One illustration of a country's unique legal and economic values is the protection of minority shareholders and employees that is available under German law but not under the laws of other EU countries. See *id.* (citing Written Observations submitted by the Commission of the European Communities pursuant to article 20(2) of the Statute of the Court of Justice of the European Communities, Aug. 30, 2000, JURM (2000) 72 CS.hg at 22). If a company were able to have its principal place of business in Germany while incorporating in another country, then it could avoid the German laws that protect minority shareholders and employees. *Id.*

seat doctrine promotes the equal treatment of corporations, as the theory requires all companies that have their place of management in a certain country to incorporate in the same state.⁵⁶ The doctrine allows host countries to remove a company's choice of law, thereby helping to prevent a race to the bottom. Companies are not able to shop around for the legal system that is most suitable to their needs while maintaining their principal places of business in other countries.⁵⁷

The incorporation theory is an alternative to the real seat doctrine.⁵⁸ It applies the law of the state of incorporation to regulate a company.⁵⁹ The state-of-incorporation doctrine promotes the incorporators' freedom of choice regarding the law that will regulate the internal affairs of their companies.⁶⁰ Advantages of the incorporation theory include "certainty, predictability, uniformity of result, protection of justified expectation of the parties," and ease of determining the applicable law.⁶¹ However, contrary to the real seat

56. See *id.* at 1027-28 (discussing the real seat doctrine's *Gleichbehandlungsgrundsatz*, or emphasis on equal treatment). Because all companies having their principal place of business in a country must incorporate in that state, these entities cannot subject themselves to less stringent rules by incorporating in another state. *Id.* Thus, they must all follow the same set of regulations—the company law of the real seat state. *Id.* at 1028.

57. See Holst, *supra* note 48, at 328; see also Ebke, *supra* note 27, at 1028 (concluding that the requirement that companies be incorporated in the state where their place of management is located produces a "level playing field and prevents companies from escaping that state's legal controls through incorporation in a jurisdiction that has less stringent laws"); Guhan Subramanian, *The Influence of Antitakeover Statutes on Incorporation Choice: Evidence on the "Race" Debate and Antitakeover Overreaching*, 150 U. PA. L. REV. 1795, 1869-70 (2002) (claiming that the seat theory represents one of the reasons why regulatory competition within the European Union is very limited).

58. See *supra* note 43 and accompanying text (explaining that the real seat doctrine and incorporation theory are two competing approaches to determining the nationality of a corporation).

59. See Kersting, *supra* note 43, at 37 (stating that the location of a company's registered office determines its nationality under the incorporation theory).

60. See Dammann, *supra* note 48, at 609 (relaying that the incorporation theory allows a company to incorporate in the state with the most desirable company law, which will then govern its internal affairs) (citing Erin A. O'Hara & Larry E. Ribstein, *From Politics to Efficiency in Choice of Law*, 67 U. CHI. L. REV. 1151, 1162 (2000)); see also Ebke, *supra* note 27, at 1028 (noting that under the state-of-incorporation doctrine, the promoters of a company can choose the legal system that is most suitable to the corporation). By comparison, under the real seat doctrine, the promoters' only choice is the company's principal place of business. *Id.*

61. Ebke, *supra* note 27, at 1031-32 (citing Deborah A. DeMott, *Perspectives on Choice of Law for Corporate Internal Affairs*, 48 L. & CONTEMP. PROBS. 161, 162 (1985) (citing RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 302 cmt. e (1971))). *But see id.* at 1032 (reporting that opponents of the incorporation doctrine note that countries that have adopted the incorporation theory have been applying local internal affairs laws, which has resulted in the application of the law of a combination of jurisdictions).

doctrine, the incorporation theory may lead to a race to the bottom, where companies seek to incorporate in the country with the least-stringent regulations while conducting their business elsewhere.⁶²

C. *The German Seat Theory Prior to Überseering*

While the real seat doctrine is generally only concerned with placing jurisdiction over a company in the courts of the seat state,⁶³ the German version of the seat theory went further. This version drastically affected the legal capacity of a foreign-incorporated entity, raising questions of compatibility with the EC Treaty.⁶⁴

When a foreign company has its central place of management in Germany, then the corporation must follow German company law.⁶⁵ However, under pre-*Überseering* German law, foreign corporations had legal capacity in Germany only if their place of management and incorporation were in the same state.⁶⁶ Companies incorporated outside of Germany and having their main seat within Germany lacked legal capacity in Germany.⁶⁷ Similarly, companies incorporated in Germany lost their legal capacity if they moved their

62. See, e.g., Dammann, *supra* note 48, at 609 (explaining that the incorporation theory may induce states to adopt “ever more management-friendly rules” to draw companies to incorporate under their jurisdiction, which will ultimately lead to a race to the bottom). The real seat doctrine, by contrast, prevents this problem by ensuring that a company’s place of incorporation and principal place of business remain the same. *Id.* at 611. Under the seat theory, a company has only a limited choice of law: if a company wants a more desirable set of corporate rules to govern its internal affairs, then it must relocate its seat to that jurisdiction—a move that is usually associated with disproportionately high costs. *Id.* See generally *infra* note 206 (juxtaposing arguments that regulatory competition will lead to a race to the bottom or a race to the top).

63. See Kersting, *supra* note 43, at 37 (indicating that the seat theory uses a company’s place of administration to determine its nationality for purposes of finding its home jurisdiction).

64. See *infra* notes 65-78 and accompanying text (discussing the German interpretation of the real seat doctrine prior to the ECJ’s ruling in *Überseering*).

65. See Ebke, *supra* note 27, at 1022 (noting that the German seat theory requires companies that have their seat in Germany to incorporate there, while a company that does not have its seat in Germany cannot incorporate under German law); see also Harald Herrmann, *How to Classify Foreign Entities in Germany*, INT’L TAX REV., Dec.-Jan. 2003, at 42, 43 (explaining the practical implications of the seat theory).

66. See Heine, *supra* note 48, at 103 (commenting that the origin of the dispute in *Überseering* lay in German company law); see also Herrmann, *supra* note 65, at 43 (detailing the meaning of the *Sitztheorie* or seat theory). See generally A.M. ARNULL ET AL., EUROPEAN UNION LAW 469 (4th ed. 2000) (noting that several Member States require that a company be incorporated in the seat state or the host state would not recognize its legal capacity).

67. See Herrmann, *supra* note 65, at 43. See generally ARNULL, *supra* note 66, at 468 (noting that Member States’ national laws can impede the move of a company’s central administration because the host country may require it to reestablish itself in the new jurisdiction). Such provisions constitute a denial of the company’s legal capacity. *Id.*

place of management abroad.⁶⁸ The result was that such companies could not bring legal actions in Germany because German law failed to recognize them as corporations.⁶⁹ The only way for those companies to acquire legal capacity in Germany was to dissolve and reincorporate in Germany.⁷⁰ Importantly, the reincorporation requirement applies only to companies incorporated outside of Germany and having their central management, that is, their main seat, in Germany.⁷¹ It does not affect foreign-incorporated companies that only seek to establish a branch or subsidiary, that is, a secondary establishment, in Germany.⁷² The policy behind the German version of the real seat doctrine is a desire to impose Germany's legal, economic, and social values on companies within its territory, including its rules on workers' participation in management and protection of minority shareholders.⁷³

According to the German version of the real seat doctrine, if a company was incorporated in a state where it did not maintain its

68. See Gert Brandner, *Vereinbarkeit der Sitztheorie mit der Niederlassungsfreiheit—Anmerkung zum Überseering-Urteil des EuGH*, at http://www.der-syndikus.de/briefings/eu/eu_025.htm (last visited June 12, 2004) (on file with the American University Law Review) (describing the repercussions of the German real seat doctrine for German companies moving their seat to another country). See generally ARNULL, *supra* note 66, at 468 (observing that under the law of some EU Member States, a company must give up its legal capacity when it transfers its headquarters or place of administration abroad).

69. See Ebke, *supra* note 27, at 1026-27 (noting that the seat theory inescapably results in the non-recognition of companies whose seat and place of incorporation are in two different states); see also Herrmann, *supra* note 65, at 43 (spelling out the practical consequences of German international company law). Importantly, the theoretical repercussions of non-recognition of a foreign corporation differ from its practical consequences. See Ebke, *supra* note 27, at 1034-35. The theoretical consequences of non-recognition include an entity's lack of access to the national courts as an active party and the loss of the limited liability status. *Id.* at 1035. However, these drastic results almost never occur because the reincorporation requirement is well-known in the business world and foreign entities have largely chosen to establish subsidiaries under German law, rather than to move the companies' real seat into Germany. *Id.* at 1035-36.

70. See Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶ 5, available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002); Heine, *supra* note 48, at 102 (explaining that under German law, foreign corporations with a seat in Germany had to liquidate and reincorporate in Germany in order to acquire legal capacity there). France, Italy, and Spain had similar conflict of law rules. *Id.*

71. Heine, *supra* note 48, at 102.

72. *Id.*

73. See Dammann, *supra* note 48, at 611-12 (remarking that it was the real seat doctrine that allowed Germany to develop its laws on workers' participation in company management because promoters were not able to circumvent those regulations by incorporating elsewhere). The seat theory also protects the interests of German creditors with respect to foreign corporations that may have been incorporated under laws that require little initial capital. See Herrmann, *supra* note 65, at 43.

principal place of business, then the real seat state could refuse to recognize the company's legal capacity.⁷⁴ *Überseering* BV had its real seat in Germany and its place of incorporation in the Netherlands.⁷⁵ According to its interpretation of the real seat doctrine, Germany refused to recognize *Überseering* BV as a corporation.⁷⁶ *Überseering* BV could gain legal capacity only if it reincorporated in Germany.⁷⁷ As a consequence, *Überseering* BV was unable to pursue its contractual claims against Nordic Construction in the German court system.⁷⁸

Before *Überseering*, a long debate persisted about whether the German real seat doctrine was consistent with the freedom of establishment under the EC Treaty.⁷⁹ The German courts' application of the seat theory to *Überseering* BV gave the European Court of Justice the opportunity to rule on this question.⁸⁰

74. See *supra* note 69 and accompanying text; see also Ebke, *supra* note 27, at 1034 (claiming that a controversial feature of the seat theory is the non-recognition of companies in the real seat state if they are incorporated elsewhere). Some commentators have suggested that the real seat doctrine imposes the non-recognition of a corporation's legal capacity as a sanction for being incorporated in the wrong place. See *id.* at 1035 (citing Bernhard Grossfeld, *Commentary*, in JULIUS VON STAUDINGER, KOMMENTAR ZUM BÜRGERLICHEN GESETZBUCH MIT EINFÜHRUNGSGESETZ UND NEBENGESETZEN: INTERNATIONALES GESELLSCHAFTSRECHT 7, 11, 105-11 (1998)).

75. See *Überseering*, 2002 E.C.R. ¶ 9 (relating that *Überseering* moved its center of administration to Germany but was still incorporated under Netherlands law).

76. See Heine, *supra* note 48, at 103 (explaining that foreign companies have legal capacity in Germany if their place of incorporation and place of management are in the same state); see also Herrmann, *supra* note 65, at 43 (outlining the aspects of German international company law that affected the *Überseering* action).

77. See, e.g., Heine, *supra* note 48, at 103 (noting that *Überseering* BV had no legal existence in Germany and therefore had no capacity to sue in German courts unless it moved its place of incorporation to Germany). But see *supra* note 69 (juxtaposing the theoretical and practical consequences of the real seat state's non-recognition of a company that is incorporated elsewhere). It is fairly easy and inexpensive for a foreign corporation to avoid the negative consequences of non-recognition by forming a subsidiary entity in Germany, rather than establishing the company's main seat there. Ebke, *supra* note 27, at 1035.

78. See Ebke, *supra* note 27, at 1035 (explaining that non-recognition of a company's legal capacity results in the inability to bring legal proceedings in the host state).

79. See *id.* at 1026 (observing that the ECJ decision in *Centros* initiated a debate about whether the real seat doctrine was compatible with the Treaty provisions on the freedom of establishment); see also Herrmann, *supra* note 65, at 43 (noting that some German legal scholars had questioned whether the seat theory, as practiced in Germany, was consistent with the EC Treaty, while others had suggested that mutual recognition of business forms within the European Union was beyond the scope of the EC Treaty).

80. See *Überseering*, 2002 E.C.R. ¶¶ 93-94 (answering the question of whether the Treaty provisions on freedom of establishment were compatible with the German seat theory).

D. European Union Law Regarding Freedom of Establishment

While corporations exist by virtue of the national law of the individual EU Member States,⁸¹ once a company exists, the EC Treaty confers certain rights on it.⁸² The freedom of establishment is one of those rights, as chapter two of the EC Treaty sets it out as a fundamental freedom.⁸³

Both natural persons and legal persons have the right of establishment.⁸⁴ Article 43 provides that “restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited.”⁸⁵ Article 48 makes the right of establishment applicable to legal persons: “Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community shall . . . be treated in the same way as natural persons who are nationals of Member States.”⁸⁶

81. See Garza, *supra* note 48, at 77 (explaining that the laws of the individual EU Member States control the internal operations of a company) (citing Werner F. Ebke, *Company Law and the European Union: Centralized Versus Decentralized Lawmaking*, 31 INT'L LAW. 961, 962 (1997)).

82. See *id.* at 77-78 (conveying that Member States may not restrict interstate trade due to the Treaty provisions on the free movement of goods, services, capital, as well as natural and legal persons); see also ARNULL, *supra* note 66, at 464 (pointing out that Article 48 of the EC Treaty vows to treat legal persons and natural persons within the European Union alike). A natural person's nationality can be equated with a company's place of incorporation, place of management, or principal place of business, which “serves as the connecting factor with the legal system of a particular [s]tate . . .” *Id.* (quoting Case 212/97, *Centros Ltd. v. Erhvervs-og Selskabsstyrelsen*, 1999 E.C.R. I-1459, I-1491, ¶ 20, [1999] 2 C.M.L.R. 551, 573 (1999)). It follows that companies gain EU rights by virtue of their national rights under incorporation just like natural persons acquire EU citizenship as a consequence of having citizenship of a Member State. See *id.* at 465.

83. See EC TREATY arts. 43-48 (outlining the right of establishment in the European Union); see also Case 81/87, *The Queen v. H.M. Treasury & Comm'rs of Inland Revenue, ex parte Daily Mail & General Trust PLC*, 1988 E.C.R. 5483, 5510, ¶ 15, [1988] 3 C.M.L.R. 713, 724 (1988) (noting at the outset that the freedom of establishment is a fundamental right in the European Community). See generally ARNULL, *supra* note 66, at 464-69 (providing an overview of the meaning of the right of establishment under EU law prior to the *Überseering* case); KAREN DAVIES, UNDERSTANDING EUROPEAN UNION LAW 144-48 (2001) (discussing the basic freedom of establishment rights provided in the EC Treaty and the exceptions to these rights); DAVID MEDHURST, A BRIEF AND PRACTICAL GUIDE TO EU LAW 139-46 (3d ed. 2001) (examining the right of establishment generally).

84. See *infra* notes 85-86 and accompanying text; see also ARNULL, *supra* note 66, at 464 (stating that Article 48 confers the right of establishment on companies and firms).

85. EC TREATY art. 43. Article 43 further states that “[s]uch prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.” *Id.* Additionally, “[f]reedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms . . .” *Id.*

86. EC TREATY art. 48. Article 48 defines “companies or firms” as “companies or

This means that corporations may establish themselves in an EU member country that is different from their state of incorporation—generally by forming an agency, branch, or subsidiary.⁸⁷ The law that applies to those companies is determined by reference to one of three connecting factors: the location of their incorporation, place of management, or principal place of business.⁸⁸ Importantly, the placing of these three connecting factors on the same level indicates that the EU does not have a preference for which law should govern a company's internal affairs—the laws of the seat state or the laws of the state of incorporation.⁸⁹

Before *Überseering*, two major cases had interpreted the meaning of the Treaty provisions on the right of establishment.⁹⁰ First, the ECJ held in *The Queen v. H.M. Treasury & Commissioners of Inland Revenue, ex parte Daily Mail & General Trust PLC* that Articles 43 and 48 do not confer a right on companies incorporated in one EU Member State to move their central place of management to another Member State.⁹¹ The ECJ examined the freedom of establishment from the perspective of the state of incorporation, which, it found, may legitimately prevent corporations from moving their place of management out of the country.⁹² Second, in *Centros v. Erhvervs-og*

firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making." *Id.*

87. See ARNULL, *supra* note 66, at 464 (referring to the ECJ's finding in *Centros* that companies and firms may exercise their freedom of establishment in another Member State through a secondary establishment) (citing *Centros*, 1999 E.C.R. at I-1491, ¶ 20, [1999] 2 C.M.L.R. at 584).

88. See *id.* (stating that these connecting factors tie the company to the laws of a Member State much like nationality ties a natural person to a particular legal system) (citing *Centros*, 1999 E.C.R. at I-1491, ¶ 20, [1999] 2 C.M.L.R. at 584).

89. See EC TREATY art. 48.

90. See Case 81/87, *The Queen v. H.M. Treasury & Comm'rs of Inland Revenue, ex parte Daily Mail & General Trust PLC*, 1988 E.C.R. 5483, [1988] 3 C.M.L.R. 713 (1988) (analyzing the ability of the state of incorporation to restrict a company's move to another Member State); Case C-212/97, *Centros v. Erhvervs-og Selskabsstyrelsen*, 1999 E.C.R. I-1459, [1999] 2 C.M.L.R. 551 (1999) (discussing a host state's inability to refuse to register a branch of a foreign entity).

91. See *Daily Mail*, 1988 E.C.R. at 5512, ¶ 25, [1988] 3 C.M.L.R. at 726 (interpreting the Treaty provision on the freedom of establishment under then-present European Community law standards). At the time of the ECJ's ruling in *Daily Mail*, Articles 52 and 58 contained the freedom of establishment provision for natural and legal persons. See *id.* at 5506, ¶ 1, [1988] 3 C.M.L.R. at 721. Articles 43 and 48 have since replaced them in the amended version of the EC Treaty due to renumbering. Ebke, *supra* note 27, at 1020.

92. See *Daily Mail*, 1988 E.C.R. at 5512, ¶ 25, [1988] 3 C.M.L.R. at 726 (answering the first question that the High Court of Justice, Queen's Bench Division, had certified to the ECJ). The matter giving rise to the ECJ's ruling involved the attempt by a company incorporated and managed in the United Kingdom to move its center of administration to the Netherlands while retaining its legal capacity in the United Kingdom. See *id.* at 5506-07, ¶¶ 2, 6, [1988] 3 C.M.L.R. at 721-22. The admitted

Selskabsstyrelsen, the ECJ dealt with an EU Member State's refusal to register a branch of a company incorporated in another Member State where that company's intent was to conduct its principal business in the host state and to escape the host state's minimum capital regulations.⁹³ Despite the company's obvious attempt to circumvent more stringent corporate rules, the ECJ held that the host state's refusal to register the branch constituted an infringement on the right of establishment and thus violated the EC Treaty.⁹⁴

In essence, the *Daily Mail* and *Centros* decisions establish that the freedom of establishment provisions allow the state where a company is incorporated to prevent that entity from moving its main seat to another Member State (primary establishment) but prohibit a host state from refusing to allow a foreign-incorporated company to establish a branch in its territory (secondary establishment).⁹⁵ It is unclear, however, to what extent these cases may be interpreted beyond their actual holdings.

reason for this intended transfer was the company's desire to avoid the payment of tax under UK law that it would incur when selling its assets and subsequently buying its own shares. *Id.* at 5507-08, ¶ 7, [1988] 3 C.M.L.R. at 722. After long and unsuccessful negotiations with the UK Treasury to obtain consent for its transfer, *Daily Mail* and *General Trust PLC* brought a legal proceeding and claimed that a company had the right to move its center of administration without prior consent from the state of incorporation pursuant to the Treaty provisions on freedom of establishment. *Id.* at 5508, ¶ 8, [1988] 3 C.M.L.R. at 722. Upon certification of questions by the English court, the ECJ pointed out that corporations exercise their freedom of establishment through establishing agencies, branches, or subsidiaries or through participating in a company's incorporation in another EU Member State. *Id.* at 5511, ¶ 17, [1988] 3 C.M.L.R. at 725. The Court ultimately held that the Treaty provisions on freedom of establishment do not bestow on a company the right to transfer its main place of management from its state of incorporation to another EU Member State. *Id.* at 5512, ¶ 25, [1988] 3 C.M.L.R. at 726.

93. See *Centros*, 1999 E.C.R. at I-1487, ¶ 2, [1999] 2 C.M.L.R. at 581 (explaining that *Centros Ltd.* had its registered office in the United Kingdom and was seeking to establish a branch in Denmark to carry on its principal business there). Both owners of *Centros Ltd.* were Danish nationals whose company had never traded in the United Kingdom. *Id.* at I-1487, ¶ 3, [1999] 2 C.M.L.R. at 581. When the Danish Trade and Companies Board refused to register a branch in Denmark, the company's owners filed an action claiming that they were entitled to establish a branch pursuant to the Treaty provisions on the freedom of establishment. *Id.* at I-1488, ¶¶ 7, 8, 10, [1999] 2 C.M.L.R. at 581-82. The Danish court sought guidance from the ECJ. *Id.* at I-1489, ¶ 13, [1999] 2 C.M.L.R. at 582.

94. See *id.* at I-1494, ¶ 30, [1999] 2 C.M.L.R. at 586 (finding that Denmark's refusal to register a branch of *Centros Ltd.* was inconsistent with the EC Treaty because it prevented a company from exercising its freedom to set up a secondary establishment).

95. See *Daily Mail*, 1988 E.C.R. at 5512, ¶ 25, [1988] 3 C.M.L.R. at 726 (holding that a company has no right to transfer its control and management to another Member State if the original Member State and place of incorporation objects); *Centros*, 1999 E.C.R. at I-1494, ¶ 30, [1999] 2 C.M.L.R. at 586 (holding that a Member State cannot refuse to register a branch of a company incorporated in another Member State).

The Treaty provisions on the freedom of establishment are relevant to the *Überseering* proceeding because *Überseering BV* was deemed under German law to have moved its seat from the Netherlands to Germany.⁹⁶ The company could thus be seen as exercising its right of establishment.

II. THE COURTS' DECISIONS IN THE *ÜBERSEERING* CASE

A. *The German Courts' Rulings*

1. *The German courts' analysis conformed to then-existing German law*

The Higher Regional Court applied the real seat doctrine in accordance with German law,⁹⁷ which meant that the law of the country where *Überseering BV* had its center of administration would determine whether it possessed legal capacity.⁹⁸ The Higher Regional Court found that the acquisition of all shares in the company by two Germans constituted a transfer of *Überseering BV*'s center of administration from the Netherlands to Germany.⁹⁹ Based on this finding and in accordance with the real seat doctrine, the Higher Regional Court correctly applied German law to the *Überseering* action.¹⁰⁰ Under German law, a foreign-incorporated company with its place of management in Germany could only acquire legal capacity if it reincorporated in Germany.¹⁰¹ Because *Überseering BV* did not reincorporate in Germany, the Higher Regional Court properly held that *Überseering BV* lacked legal capacity and could

96. See Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶¶ 7, 9, available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J028 (Nov. 5, 2002).

97. See *id.* ¶ 4 (mentioning that the company seat principle is established in the German High Court's case law and that most legal commentators in Germany approve of it); see also Ebke, *supra* note 27, at 1022-23 (noting the consistent application of the real seat doctrine in Germany).

98. See *Überseering*, 2002 E.C.R. ¶¶ 4, 9 (conveying that Germany follows the seat theory, which applies the laws of the country where the company has its center of administration).

99. See *id.* ¶¶ 7, 9 (commenting that a Higher Regional Court in Germany found that *Überseering BV*'s actual center of administration was in Düsseldorf, Germany). The governments of the Netherlands and the United Kingdom as well as the European Free Trade Association ("EFTA") Surveillance Authority maintained in their submissions to the ECJ that *Überseering BV* did not intend to move its center of administration to Germany, given the consequences of such a transfer under German law. *Id.* ¶ 48.

100. See *supra* note 98 and accompanying text.

101. See discussion *supra* Part I.C (examining the German seat theory prior to the *Überseering* decision).

not bring legal actions in Germany.¹⁰² The holding of the German courts certainly conformed to then-existing German law.¹⁰³

2. *The German courts' analysis conformed to ECJ precedent*

The reasoning of the German courts was also proper with respect to then-existing EU law.¹⁰⁴ After the ECJ's rulings in *Daily Mail* and *Centros*, the consensus among German legal commentators was that the ECJ found the real seat doctrine to be compatible with the Treaty provisions on freedom of establishment.¹⁰⁵ Because the ECJ's previous rulings on the freedom of establishment in *Daily Mail* and *Centros* did not provide sufficient guidance to decide the *Überseering* case,¹⁰⁶ the German Federal Court of Justice was justified in seeking clarification on the applicable conflict-of-laws principles.¹⁰⁷

102. See *Überseering*, 2002 E.C.R. ¶ 9 (observing that the Higher Regional Court determined that Germany could not recognize *Überseering BV*'s legal capacity as a company incorporated in the Netherlands but having its place of management in Germany).

103. See § 50 Nr. 1 ZPO (German Code of Civil Procedure) (providing that an entity may be an active party to a legal proceeding if it has legal capacity); see also *Überseering*, 2002 E.C.R. ¶ 3 (relating that the German Code of Civil Procedure requires an action to be dismissed if it was initiated by a party that does not have legal capacity). See generally discussion *supra* Part I.C (discussing the German seat theory before *Überseering*).

104. See *infra* notes 105-19 and accompanying text (highlighting the gaps in EU corporate conflict-of-laws rules prior to *Überseering*).

105. See, e.g., Ebke, *supra* note 27, at 1018-20 (relaying the pre-*Überseering* consensus that Germany was not required to recognize a foreign-incorporated company's legal capacity under international law); Garza, *supra* note 48, at 78 (noting that the requirement of reincorporation in the seat state was legitimate under pre-*Überseering* EU company law); see also SLAVICA VANOVAČ, HAARMANN HÜGEL, EUGH: VERSTOB DER SITZTHEORIE GEGEN DEN EG-VERTRAG: ART. 43, 48, 293 EGV; ÜBERSEERING/NCC, at <http://www.hugelaw.com/new/texte/wi03sitztheorie.html> (2004) (on file with the American University Law Review) (clarifying that the ECJ corrected that interpretation of *Daily Mail* in its *Überseering* ruling). See generally Holst, *supra* note 48, at 327 (relating that some scholars contend that *Centros* abolished the real seat doctrine, while others maintain that the decision only concerned the freedom of secondary establishment) (citing Werner Ebke, *Centros: Some Realities and Some Mysteries*, 48 AM. J. COMP. L. 623, 627 (2000); Wulf-Henning Roth, *Case Note*, 37 COMMON MKT. L. REV. 147 (2000)); Heine, *supra* note 48, at 103 (explaining that the ECJ in *Centros* did not rule on whether the incorporation theory or the real seat doctrine was to be the governing conflict-of-laws principle in the European Union).

106. See Judgment of March 30, 2000, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718, ¶ 42 (declaring that the answer to whether the application of the real seat doctrine in the *Überseering* case would be consistent with the freedom of establishment could not be directly deduced from the ECJ's prior rulings in *Daily Mail* and *Centros*). See generally *supra* note 105.

107. See *Überseering*, 2002 E.C.R. ¶ 21 (reciting the two questions that the German Federal Court of Justice certified to the ECJ); see also *infra* note 119 (describing the procedure for obtaining a preliminary ruling from the ECJ). The German Federal Court of Justice stayed proceedings while waiting for the ECJ's preliminary ruling on the matter. *Überseering*, 2002 E.C.R. ¶ 21.

Neither *Daily Mail* nor *Centros* directly addressed *Überseering* BV's situation. *Daily Mail* concerned the ability of the state of incorporation to restrict a company's move to another Member State,¹⁰⁸ and *Centros* dealt with a host state's inability to refuse to register a branch of a foreign entity.¹⁰⁹ The *Überseering* case, by contrast, involved a host state's refusal to recognize a foreign company's legal capacity when that entity had moved its central place of management to the host state.¹¹⁰ The *Daily Mail* decision was not applicable to the *Überseering* case¹¹¹ because the former concerned the relationship between a company and the incorporation state, whereas the latter raised questions about the powers of the seat state.¹¹²

The ECJ's ruling in *Centros* was also not directly on point since *Centros Ltd.* had sought to establish a branch in another EU Member State, while the owners of *Überseering* BV never intended to establish a branch.¹¹³ Instead, *Überseering* BV was deemed under German law to have moved its center of administration and control to Germany—a primary establishment rather than a branch.¹¹⁴ Because the previous case law of the ECJ did not address the legal question in *Überseering*,¹¹⁵ the Higher Regional Court was likely justified in its decision to apply the German seat theory, which resulted in the denial of *Überseering* BV's legal capacity.

108. Case 81/87, *The Queen v. H.M. Treasury & Comm'rs of Inland Revenue, ex parte Daily Mail & General Trust PLC*, 1988 E.C.R. 5483, 5506, ¶ 1, [1988] 3 C.M.L.R. 713, 721 (1988).

109. Case C-212/97, *Centros Ltd. v. Erhvervs-og Selskabsstyrelsen*, 1999 E.C.R. I-1459, I-1490, ¶ 16, [1999] 2 C.M.L.R. 551, 583 (1999).

110. See discussion *supra* Part I.A (detailing the facts and procedural history of the *Überseering* case).

111. See *Überseering*, 2002 E.C.R. I-9919, ¶¶ 62-71 (discussing the differences between the situation in *Daily Mail* and that in *Überseering*); *VANOVAC*, *supra* note 105 (contending that the relations between a company and its state of incorporation, which were at issue in *Daily Mail*, are regulated pursuant to the law of the incorporation state). Accordingly, the *Daily Mail* decision does not contain any revelations about the compatibility of the real seat doctrine and the freedom of establishment. *Id.*

112. Compare *Daily Mail*, 1988 E.C.R. 5483, [1988] 3 C.M.L.R. 713 (analyzing the right of the state of incorporation to restrict a company's ability to move its center of management and control out of the country), with *Überseering*, 2002 E.C.R. I-9919 (evaluating the power of the seat state to deny a foreign company's legal capacity).

113. Compare *Centros*, 1999 E.C.R. at I-1487, ¶¶ 2-3, [1999] 2 C.M.L.R. at 581 (noting that the owners of *Centros Ltd.* had requested Danish authorities to register a branch of the company, which they refused to do), with *Überseering*, 2002 E.C.R. ¶¶ 7, 9 (recounting that the acquisition by German nationals of all shares in *Überseering* BV constituted a transfer of the company's management seat).

114. *Überseering*, 2002 E.C.R. ¶¶ 7, 9.

115. See discussion *supra* Part I.D (describing the ECJ's decisions in *Centros* and *Daily Mail* on freedom of establishment in the European Union); see also *supra* note 105 and accompanying text (summarizing the pre-*Überseering* consensus among legal scholars that the seat theory was compatible with the freedom of establishment).

An argument could be made, however, that the distinction between the situation in *Centros* and that in *Überseering* is artificial and irrelevant, as it assumes a significant difference between the formation of a secondary versus primary establishment.¹¹⁶ If the German courts had not imputed artificial relevance into the distinction between *Centros* and *Überseering*, they would arguably have had to recognize that *Centros* demands that Germany accept the legal capacity of *Überseering* BV.¹¹⁷ On the other hand, the establishment of a branch has less significant implications for the host state than does the transfer of the company's seat. It seems reasonable to allow a host state to exert greater control over companies that have their seat and carry on their primary business within that country than over corporations that have merely established a branch there.

Due to the lack of clarity in then-existing EU law,¹¹⁸ the German Federal Court of Justice was certainly justified in asking the ECJ for guidance on the matter.¹¹⁹ The German court first asked the ECJ to

116. See Holst, *supra* note 48, at 329 (concluding that the ECJ defined the term "branch" so broadly in its *Centros* ruling that it would essentially represent a "seat" in the view of the states that follow the real seat doctrine). Compare *Centros*, 1999 E.C.R. at I-1487, ¶ 2, [1999] 2 C.M.L.R. at 581 (relaying that the dispute arose out of Denmark's refusal to register a branch of *Centros* Ltd.—a secondary establishment), with *Überseering*, 2002 E.C.R. ¶¶ 6-10 (observing that the ECJ's review of the *Überseering* matter sprang from a German court's denial of *Überseering* BV's legal capacity as a consequence of the company's transfer of its place of management and control—the founding of a primary establishment).

117. See *Centros*, 1999 E.C.R. at I-1494, ¶ 30, [1999] 2 C.M.L.R. at 586 (holding that a host country's refusal to register a branch of a foreign-incorporated entity violates the Treaty provisions on freedom of establishment).

118. See ARNULL, *supra* note 66, at 466-69 (describing the confusion about the meaning of the ECJ's rulings in *Daily Mail* and *Centros*); see also Werner Ebke, *Centros: Some Realities and Some Mysteries*, 48 AM. J. COMP. L. 623, 629 (2000) (contending that the ECJ's case law on what amounts to an illegitimate restriction on the freedom of primary or secondary establishment is inconsistent and does not always allow for logical deduction of a rule for every situation that may arise in this area). Part of the problem with interpreting the ECJ precedent is that legal scholars have speculated far beyond the Court's actual holdings in *Daily Mail* and *Centros* in an effort to bring light to some of the unclear language and ambiguous statements in the Court's dicta. *Id.*

119. See ARNULL, *supra* note 66, at 200-02 (explaining that parties may ask the ECJ for a preliminary ruling under Article 234 of the EC Treaty). Article 234 provides in relevant part:

The Court of Justice shall have jurisdiction to give preliminary rulings concerning:

(a) the interpretation of this Treaty; . . .

Where such a question is raised before any court or tribunal of a Member State, that court or tribunal may, if it considers that a decision on the question is necessary to enable it to give judgment, request the Court of Justice to give a ruling thereon.

EC TREATY art. 234. Because the ECJ is not bound by previous decisions, national courts may ask for clarification or preliminary judgments despite the fact that a previous ECJ judgment may be binding precedent on the issue before the national court. See ARNULL, *supra* note 66, at 200-02.

determine whether the application of the real seat doctrine is inconsistent with the Treaty provisions on the freedom of establishment if it leads to the non-recognition of a foreign-incorporated company.¹²⁰ In the event the ECJ answered the first question in the affirmative, the German Federal Court of Justice asked whether legal capacity would have to be determined with reference to the laws of the state of incorporation.¹²¹

B. *The ECJ's Judgment*

The ECJ properly concluded that a host state's denial of the legal capacity of a company incorporated in another EU Member State constitutes an illegitimate restriction on the freedom of establishment.¹²² However, the Court failed to provide sufficient guidance on the circumstances under which a restriction on the freedom of establishment may be justified.¹²³

The ECJ analyzed the *Überseering* matter pursuant to its authority under Article 234 of the EC Treaty.¹²⁴ It reviewed the case under a

120. The court presented the question:

Are Articles 43 EC and 48 EC to be interpreted as meaning that the freedom of establishment of companies precludes the legal capacity, and capacity to be a party to legal proceedings, of a company validly incorporated under the law of one Member State from being determined according to the law of another State to which the company has moved its actual centre of administration, where, under the law of that second State, the company may no longer bring legal proceedings there in respect of claims under a contract?

Überseering, 2002 E.C.R. ¶ 21.

121. The court asked: "Does the freedom of establishment of companies (Articles 43 EC and 48 EC) require that a company's legal capacity and capacity to be a party to legal proceedings is to be determined according to the law of the State where the company is incorporated?" *Id.*

122. See discussion *infra* Parts II.B.2 and II.B.3 (analyzing the ECJ's findings regarding whether a restriction on the freedom of establishment had occurred in the *Überseering* case and whether a justification for the restriction existed).

123. See *infra* note 192 and accompanying text.

124. See EC TREATY art. 234 (establishing that Member States may request a preliminary ruling from the ECJ when such a ruling is necessary in order for them to render a judgment); *supra* note 119 and accompanying text; see also ARNULL, *supra* note 66, at 264 (observing that allowing the national courts of Member States to seek preliminary rulings from the ECJ under Article 234 is essential to the proper functioning of the common market because it ensures that EU law will be interpreted and applied the same way in all Member States). Since 1989, the Court of First Instance of the European Communities has been interpreting European Community law, a task originally performed solely by the ECJ. *Id.* at 191. Interpreting European Community law is complicated by the "multilingual nature of European Community law." *Id.* at 198. Thus, "[t]he interpretation of Community instruments involves very often not the process familiar to common lawyers of laboriously extracting the meaning from words used but the more creative process of applying flesh to a spare and loosely constructed skeleton." *Id.* (quoting Commissioners of Customs and Excise v. *Samex ApS*, 3 C.M.L.R. 194, 211 (Q.B.D. Comm. Ct. 1983) (U.K.)).

three-step analysis. First, it addressed the question of whether the Treaty provisions concerning the freedom of establishment applied in the *Überseering* case.¹²⁵ Second, the ECJ analyzed whether a restriction on the freedom of establishment had occurred.¹²⁶ Third, the Court inquired whether a justification existed for that restriction.¹²⁷ The ECJ ultimately held that the Treaty provisions on the freedom of establishment require host states to recognize the legal capacity of a company and allow it access to the national courts, where the company is incorporated in one EU Member State and moves its center of administration to another Member State.¹²⁸

1. *The Treaty provisions on freedom of establishment apply*

Regarding the applicability of the Treaty provisions on freedom of establishment, the ECJ properly found that they cover a host country's legal treatment of a foreign corporation.¹²⁹ In their submissions to the Court, Nordic Construction and the governments of Germany, Spain, and Italy argued that the real seat doctrine is compatible with the Treaty provisions on freedom of establishment, even if it leads to the denial of the legal capacity of a foreign corporation.¹³⁰ By contrast, *Überseering BV*, the governments of the Netherlands and United Kingdom, the Commission, and the

125. See *Überseering*, 2002 E.C.R. ¶¶ 52-77 (determining that a foreign corporation may rely on the freedom of establishment, which is ensured under the EC Treaty, to challenge a Member State's refusal to recognize its legal capacity). The Court also pointed out that the Treaty provisions on the free movement of capital would apply to a person's acquisition of shares in a foreign corporation. *Id.* ¶ 77. By contrast, the Treaty provisions on freedom of establishment apply when that person acquires all shares in a company that is incorporated in another Member State and when that person can then determine the company's activities. *Id.*

126. See *id.* ¶¶ 78-82 (finding that the application of the German seat theory had indeed resulted in a restriction of the freedom of establishment). The Court also noted that requiring a foreign company to reincorporate in Germany once it had moved its place of administration there constitutes an "outright negation of freedom of establishment." *Id.* ¶ 81.

127. See *id.* ¶¶ 83-92 (examining whether the restriction on the freedom of establishment was justified by its lack of discrimination, its proportionality, and its important role in achieving public policy goals).

128. See *id.* ¶¶ 94-95 (finding a host state's nonrecognition of a foreign-incorporated company's legal capacity to be incompatible with the Treaty provisions on freedom of establishment).

129. See *id.* ¶ 52 (declaring that a company validly incorporated in one Member State which is deemed by a second Member State to have moved its seat to the second state is still covered by the Treaty provisions regarding the freedom of establishment).

130. See *id.* ¶ 23-35 (summarizing the argument of Nordic Construction and the German, Spanish, and Italian governments that the freedom of establishment provisions do not prevent the laws of the host state from determining the legal capacity of a company that is incorporated elsewhere and moves its real seat to the host state).

European Free Trade Association (“EFTA”)¹³¹ Surveillance Authority took the position that Articles 43 and 48, taken together, preclude the host state from determining the legal capacity of a company according to its laws.¹³²

Nordic Construction, Germany, Spain, and Italy based their arguments in part on Article 293 of the EC Treaty, which provides in relevant part:

Member States shall, so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals . . . the mutual recognition of companies or firms within the meaning of . . . Article 48, [and] the retention of legal personality in the event of transfer of their seat from one country to another. . . .¹³³

The government of Italy noted that Article 293 specifically states that negotiations between states should be the mechanism for determining how corporate personhood is retained upon seat transfers across boundaries.¹³⁴ According to the Commission, however, the requirement under Article 293 that “Member States shall, so far as is necessary, enter into negotiations” has been made unnecessary by the body of ECJ case law that has developed since the signing of that Article in 1968.¹³⁵

131. See PHILLIP RAWORTH, INTRODUCTION TO THE LEGAL SYSTEM OF THE EUROPEAN UNION 3 (2001) (detailing the functions and history of the EFTA). The EFTA was first established by the United Kingdom as a rival trade grouping to the European Economic Community in 1960. *Id.* It allowed those states that did not wish to join the European Community to establish their own free trade zone. See ARNULL, *supra* note 66, at 9-10.

132. See *Überseering*, 2002 E.C.R. ¶¶ 36-51 (setting forth the main arguments of *Überseering BV*, the governments of the Netherlands and United Kingdom, the Commission, and the EFTA Surveillance Authority).

133. EC TREATY art. 293; see *Überseering*, 2002 E.C.R. ¶ 24.

134. *Überseering*, 2002 E.C.R. ¶ 27. Spain commented that the Convention on the Mutual Recognition of Companies and Legal Persons was signed in 1968, but never entered into force. *Id.* ¶ 28. Therefore, Article 293 has not been fulfilled by negotiations, and articles 43 and 48 are silent as to the relevant questions. *Id.* Thus, Spain argued that there is no real consensus among Member States as to what are the legal ramifications for a company that moves its seat. *Id.* Similarly, Nordic Construction submitted that no freedom of establishment violations had occurred because the articles envision negotiations between Member States to set up a framework of mutual recognition of companies, which has not yet occurred. See *id.* ¶ 25. Moreover, companies are still free to either reincorporate themselves or establish a presence in a host state as long as their largest center of administration and their place of incorporation remain in the same state. *Id.* Germany argued that Articles 43 and 48 were written to allow national control over corporate law until the accomplishment of legal harmonization. *Id.* ¶ 26. Because harmonization has not yet occurred, the argument continues, German real seat practice and its implications for the legal capacity of corporations are legal under the EC Treaty. *Id.*

135. See *id.* ¶ 37 (recounting the Commission’s contrary interpretation of Article 293).

In its findings, the ECJ disagreed with the arguments of Nordic Construction and its supporting governments and stated that the laws which the host state applies to a foreign-incorporated company fall within the freedom of establishment provisions.¹³⁶ The Court specifically rejected the arguments concerning Article 293 of the EC Treaty because Articles 43 and 48 by themselves allow companies to exercise their freedom of establishment.¹³⁷ Entities cannot exercise that right of establishment if host states will not recognize them as companies.¹³⁸

Nordic Construction and its supporting governments also cited *Daily Mail* to support their proposition.¹³⁹ In *Daily Mail*, the ECJ indicated that whether and how a seat transfer may happen is “not resolved by the rules concerning the right of establishment but must be dealt with by future legislation or conventions.”¹⁴⁰ *Überseering BV* and its supporting governments and institutions, on the other hand, argued that *Daily Mail* is inapplicable because in that case the ECJ only ruled on the effect of a real seat transfer in the state of incorporation rather than in the host state.¹⁴¹ Instead, they saw greater applicability in the ECJ’s ruling in *Centros* because it dealt with the law of the host state.¹⁴²

136. See *id.* ¶ 52 (finding that the freedom of establishment provisions cover a host state’s application of its laws to a company that is incorporated in another EU Member State and has transferred its center of administration to the host country).

137. See *id.* ¶¶ 53-60 (rejecting the argument that Article 293 requires negotiations between states or the adoption of a convention to be the basis for mutual recognition of companies that transfer seats to other Member States).

138. See *id.* ¶ 59 (characterizing host states’ recognition of companies as “[a] necessary precondition for the exercise of the freedom of establishment”).

139. See *id.* ¶ 29 (citing Case 81/87, *The Queen v. H.M. Treasury & Comm’rs of Inland Revenue, ex parte Daily Mail & General Trust PLC*, 1988 E.C.R. 5483, 5512, ¶¶ 23-24, [1988] 3 C.M.L.R. 713, 726 (1988)).

140. *Überseering*, 2002 E.C.R. ¶ 29 (quoting *Daily Mail*, 1988 E.C.R. at 5512, ¶ 23-24, [1988] 3 C.M.L.R. at 726). Germany argued that *Daily Mail* applied to the facts of *Überseering* even though the controversy in *Daily Mail* was between a company and its state of incorporation rather than with its host state. *Überseering*, 2002 E.C.R. ¶ 30.

141. See *Überseering*, 2002 E.C.R. ¶¶ 38-39 (discussing the attempt by *Überseering BV*, the Netherlands, the United Kingdom, the Commission, and the EFTA Surveillance Authority to distinguish *Daily Mail* from the facts in *Überseering*). They argued that *Daily Mail* states that companies are creatures of national law and thus may be regulated by their state of incorporation. *Id.* ¶ 40. However, the ECJ did not determine in that case whether a company must be regulated or recognized in a second state. *Id.*

142. See *id.* ¶¶ 41-43. In *Centros*, the ECJ decided that the host state must allow a company incorporated in another Member State to freely establish a branch in the host country even when it is clear that the company would conduct the majority of its business in the host country and that the parent corporation is merely a legal strategy to avoid the laws of the host country. *Id.* ¶¶ 42-43.

The ECJ addressed these two contrary interpretations of its earlier ruling in *Daily Mail*.¹⁴³ Again, the Court agreed with the submissions of *Überseering BV* and its supporting governments and institutions and held that *Daily Mail* is distinct from *Überseering*.¹⁴⁴ The ECJ stated that *Daily Mail* did not deal with the question of whether a host state is able to deny legal capacity to a company that is incorporated in one EU Member State and has moved its seat to the host state.¹⁴⁵ Thus, the Court reasoned that *Daily Mail* did not provide guidance for the *Überseering* case, where the Court would have to decide whether a host state has the right to deny a company's legal capacity upon that entity's seat transfer to the host state.¹⁴⁶ The ECJ concluded that *Überseering BV* could base its arguments on Articles 43 and 48, which guarantee the right of establishment.¹⁴⁷

2. *A restriction on the freedom of establishment occurred*

Once the Court determined that the Treaty provisions on freedom of establishment applied to the *Überseering* case, it examined whether Germany violated those principles by refusing to recognize *Überseering BV*'s legal capacity.¹⁴⁸ The Court's reasoning centered on the realization that German law forces a foreign-incorporated company that has moved its center of administration to Germany to reincorporate in Germany if it seeks to file a legal action there.¹⁴⁹ The ECJ focused heavily on the implications of that reincorporation requirement.¹⁵⁰ The Court seemed to imply that the right of establishment becomes meaningless if the company does not enjoy legal recognition and the ability to bring court actions in the host

143. *See id.* ¶¶ 61-73.

144. *See id.* ¶¶ 62-71 (observing that *Daily Mail* addressed the relationship between companies and their states of incorporation when the companies transfer their administrative centers to another state, while *Überseering* addressed the relationship between companies and their host states).

145. *See id.* ¶¶ 70-71 (distinguishing the limited holding of the *Daily Mail* decision from the questions presented in *Überseering*). The ECJ stated that the *Daily Mail* case only determined that a company's state of incorporation may restrict that company's ability to move its management seat abroad. *Id.* ¶ 70.

146. *Id.* ¶¶ 71-72.

147. *See id.* ¶¶ 76-77 (finding that the application of the German real seat doctrine and resulting denial of *Überseering BV*'s legal capacity fall within the scope of the Treaty provisions on freedom of establishment).

148. *See id.* ¶¶ 52-77.

149. *See id.* ¶ 79 (“[A] company validly incorporated under the law of . . . a Member State other than . . . Germany has under German law no alternative to reincorporation in Germany if it wishes to enforce before a German court its rights under a contract entered into with a company incorporated under German law.”).

150. *See id.* ¶¶ 79, 81-82 (discussing the negative ramifications that the denial of a foreign-incorporated company's legal capacity and ability to bring legal proceedings will have on the freedom of establishment).

state.¹⁵¹ In fact, the host state's recognition of the company's legal capacity is a necessary precondition to the exercise of the freedom of establishment.¹⁵² Without legal recognition and, particularly, the ability to bring legal proceedings, the formation of a secondary or primary establishment lacks a legal basis.¹⁵³ Based on this insightful observation, the Court correctly reasoned that the denial of a company's legal capacity, which resulted from the application of the German seat theory, constituted a negation of the freedom of establishment.¹⁵⁴

To support its finding, the ECJ pointed out that *Überseering BV* did not lose its standing as an entity incorporated in the Netherlands when two German nationals acquired all shares of the company.¹⁵⁵ Further, the Court relied on its ruling in *Daily Mail* to contend that "a company exists only by virtue of the national legislation which determines its incorporation and functioning."¹⁵⁶ The Court noted that *Überseering BV* had the right to exercise its freedom of establishment under the EC Treaty.¹⁵⁷ Thus, the ECJ concluded that Germany's refusal to recognize *Überseering BV*'s legal capacity and denial of court access were inconsistent with the Treaty provisions on freedom of establishment.¹⁵⁸

3. *The restriction on the freedom of establishment was not justified*

Perhaps the greatest significance of the *Überseering* case lies in the ECJ's discussion of the possible justifications for a restriction on the right of establishment. While finding the non-recognition of a

151. See *id.* ¶¶ 78-82 (observing that *Überseering BV* existed as a company under Netherlands law and that Germany's requirement that it reincorporate in Germany upon moving its seat to the country constituted a negation of *Überseering BV*'s freedom of establishment).

152. See Elisabeth M. Mayr, *Überseering: Das Ende der Sitztheorie?*, at <http://www.juralotse.de/newsletter/nl57-003.shtml> (Sept. 19, 1999) (on file with the American University Law Review) (stating that the freedom of establishment requires legal recognition by all EU Member States where the entity may wish to exercise its right of establishment).

153. See *Überseering*, 2002 E.C.R. ¶ 81 ("The requirement of reincorporation . . . is . . . tantamount to outright negation of freedom of establishment.").

154. See *id.* ¶¶ 80-81.

155. See *id.* (claiming that *Überseering BV* has the right to exercise its freedom of establishment because "its very existence is inseparable from its status as a company incorporated under Netherlands law" and that it did not lose its legal personhood in the Netherlands even when German citizens purchased all of its shares).

156. *Id.* ¶ 81.

157. See *id.* ¶ 80 (stating that Articles 43 and 48 of the EC Treaty entitle a company incorporated in one EU Member State to exercise its freedom of establishment in another Member State).

158. See *id.* ¶ 82 (declaring that the denial of access to the host country's legal system after a foreign-incorporated entity moves its center of administration to the host country constitutes a restriction on the freedom of establishment).

foreign-incorporated company to be an excessive measure, the Court acknowledged a host state's interest in regulating entities based within its territory.¹⁵⁹

Under certain circumstances, a restriction on the freedom of establishment may be justified.¹⁶⁰ The German government argued that the restrictive measures at issue in *Überseering* were covered by the public interest exception.¹⁶¹ The ECJ had previously established four conditions which a restriction on the exercise of a fundamental freedom must fulfill in order to be justified on public interest grounds.¹⁶² First, the restrictive measure must not discriminate.¹⁶³ Second, an overriding consideration of the public interest must justify the restriction.¹⁶⁴ Third, the rules must be appropriate for achieving the stated objective.¹⁶⁵ Lastly, the restriction must not exceed the measures that are necessary to achieve the objective.¹⁶⁶

Regarding the non-discriminatory application of the restrictive measure, Germany maintained that the consequences of the real seat doctrine apply both to foreign-incorporated entities that have their place of administration in Germany and to companies incorporated in Germany that move their center of administration abroad.¹⁶⁷ With respect to the requirement that the restriction be justified by superseding requirements of the public interest, the German Government pointed out several aspects of the real seat doctrine that

159. See *id.* ¶ 92 (noting that the protection of the interests of creditors, minority shareholders, employees, and taxation authorities could in some instances justify restrictions on the freedom of establishment).

160. See, e.g., DAVIES, *supra* note 83, at 147-48 (summarizing the exceptions to the right of establishment pursuant to articles 45 (official authority exception), 46 (public policy, public service, and public health exception), and 30 (public interest exception) of the EC Treaty).

161. See EC TREATY art. 46 (allowing Member States to impose limited restrictions on the freedom of establishment for public policy reasons); *Überseering*, 2002 E.C.R. ¶ 84 (reciting the German government's argument that the restriction does not violate the EC Treaty because it "applies without discrimination, is justified by overriding requirements relating to the general interest and is proportionate to the objectives pursued").

162. See Case C-55/94, *Gebhard v. Consiglio*, 1995 E.C.R. I-4165, I-4197-98, ¶ 37, [1996] 1 C.M.L.R. 603, 628 (1995) (listing the four conditions that must be satisfied to justify any national measure that potentially hinders the exercise of fundamental freedoms guaranteed by the EC treaty).

163. *Id.*

164. *Id.*

165. *Id.*

166. *Id.*

167. See Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶ 85 (relating Germany's contention that the real seat doctrine applies to foreign and native corporations alike), available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002).

are consistent with public interest considerations.¹⁶⁸ First, Germany claimed that EU law has previously acknowledged the value of having a company's center of administration coincide with its state of incorporation.¹⁶⁹ Further, the German Government argued that the German seat theory promotes legal certainty and creditor protection.¹⁷⁰ The government of Germany particularly stressed the fact that the EU Member States have not yet harmonized their laws regarding minimum capital requirements for limited liability companies.¹⁷¹ Moreover, the German Government alerted the Court to the protection of minority shareholders, employees, and joint management that a uniform application of German law guarantees.¹⁷² It expressed concern about the possibility of circumventing these rules by simply incorporating in another Member State.¹⁷³ Lastly, Germany claimed that fiscal reasons also justified a restriction on the freedom of establishment in the present case.¹⁷⁴

The Court found that no justification exists for a host state's complete denial of the legal capacity of a company that is validly incorporated in one EU Member State and moves its seat to the host country.¹⁷⁵ However, the ECJ did not entirely dismiss Germany's public interest arguments and specifically stated that "overriding requirements relating to the general interest, such as the protection

168. *See id.* ¶¶ 86-90.

169. *See id.* ¶ 86 (recounting the German Government's contention that other areas of EC law have "recognized the merits, in principle, of a single registered and administrative office" by assuming that such offices are one and the same).

170. *See id.* ¶ 87 (relaying Germany's arguments that a uniform application of Germany's private international company law to all companies whose principal place of business is in Germany will create uniform legal requirements and will give creditors and other contracting parties greater protection than they typically receive from Member States with less stringent requirements).

171. *See id.* (conveying Germany's concern that contract parties and creditors of limited liability companies receive less protection from some Member States that have significantly lower standards).

172. *See id.* ¶¶ 88-89 (describing the German Government's view that the German seat theory serves the public interest by precluding companies with their principal place of business in Germany from circumventing the national company formation requirements).

173. *See id.* ¶ 89 (summarizing Germany's contention that incorporation under the laws of another Member State could allow a company in Germany to avoid German company laws, including provisions regarding employee rights).

174. *See id.* ¶ 90 (explaining that the state-of-incorporation theory permits companies to enjoy concurrent tax advantages in all of their places of residence); *see also* Anno Rainer et al., *Compensation for ACT not Offset by Entitlement to Tax Credits*, INT'L TAX REV., Feb. 2003, at 43 (forecasting that the ECJ's holding in *Überseering*, requiring host states to recognize foreign-incorporated entities, will provide "tax planning opportunities for the use of dual resident companies in Europe"), available at <http://www.legalmediagroup.com/internationaltaxreview/default.asp?Page=3&cIindex=20&SID=2357&M=2&Y=2003>.

175. *See Überseering*, 2002 E.C.R. ¶ 93 (finding that a complete denial of legal capacity contradicts companies' guaranteed freedom of establishment).

of the interests of creditors, minority shareholders, employees and even the taxation authorities, may, in certain circumstances and subject to certain conditions, justify restrictions on freedom of establishment.¹⁷⁶

When analyzing the ECJ's finding, it is important to bear in mind that the application of the German seat theory infringed on a company's fundamental right to remedies and essentially resulted in the complete negation of the company's freedom of establishment.¹⁷⁷ The denial of a company's legal capacity and ability to bring legal proceedings constitutes an excessive measure to achieve the objective of protecting the host country's legal, economic, and social values.¹⁷⁸ A host country can protect the interests of creditors, minority shareholders, and employees through less restrictive means, such as the imposition of minimum requirements for conducting business in the host state.¹⁷⁹ Based on the Court's reasoning, it seems entirely possible that the ECJ may decide a future case more favorably for the real seat doctrine if it involves an attempt by a host country to impose its corporate regulations on the foreign company without denying the company's legal capacity.¹⁸⁰ The Court may find such regulations

176. *Id.* ¶ 92. The ECJ has not defined what may amount to an overriding requirement of the public interest but makes such determinations on a case-by-case basis. Dammann, *supra* note 48, at 651-52. In the past, the Court has found the following goals to constitute such imperative requirements: controlling unfair market practices, effectively supervising financial concerns, protecting consumers, and safeguarding media diversity. *See id.* at 652-54 (observing that the ECJ's prior findings do not constitute an exhaustive list).

177. *See* discussion *supra* Part II.B.2 (analyzing the ECJ's finding that the freedom of establishment lacks meaning when a law forces a foreign-incorporated company to reincorporate in order to receive legal recognition).

178. *See* VANOVAC, *supra* note 105 (asserting that the non-recognition of a foreign-incorporated entity is not merely a restriction on the freedom of establishment but constitutes an illegitimate negation of that right); *see also* Mayr, *supra* note 152 (commenting that the objective of protecting the rights of creditors and employees cannot justify the denial of a company's legal capacity and ability to bring legal proceedings).

179. *See* Dammann, *supra* note 48, at 623 (claiming that the imposition of Germany's codetermination provisions, unlike the Danish measures at issue in *Centros*, would not result in the negation of a company's right of establishment but would merely allow the host state to control the internal affairs of companies that conduct business in its territory); *see also* Case C-212/97, *Centros Ltd v. Erhvervs-og Selskabsstyrelsen*, 1999 E.C.R. I-1484, I-1496, ¶ 37, [1999] 2 C.M.L.R. 551, 587 (1999) (theorizing that a host country can protect creditors through less restrictive means than the refusal to register a branch of a foreign-incorporated company). In *Centros*, the Court noted that Denmark could have passed legislation to provide public creditors with the needed guarantees from the company, thus implying that such a measure would not violate the freedom of establishment provisions. *Id.*

180. *See supra* note 179 and accompanying text; *see also* Mayr, *supra* note 152 (declaring that under the ECJ ruling in *Überseering*, important considerations of the public interest may justify a restriction on the freedom of establishment under certain circumstances); VANOVAC, *supra* note 105 (inferring from the ECJ ruling in *Überseering* that overriding concerns regarding the public interest could justify a

to constitute a legitimate restriction on the freedom of establishment, provided the regulations do not result in an outright negation of the right.¹⁸¹

4. *Assessment of the ECJ's overall holding*

The ECJ ultimately held that when a company incorporated in one EU Member State moves its place of administration to another Member State, then the host country must recognize the company's legal capacity and allow it access to the host country's courts.¹⁸² In answering the first certified question, the Court found that Articles 43 and 48 *preclude* the host state from refusing to recognize the legal capacity of such a company and denying the company court access in the host country.¹⁸³ In answering the second question, the ECJ stated that the Treaty provisions on freedom of establishment *require* the host state to recognize a foreign-incorporated company's legal capacity and to grant that company access to its courts.¹⁸⁴

Interestingly, the ECJ's preliminary ruling in *Überseering* did not directly respond to the questions that the German Federal Court of Justice referred to it.¹⁸⁵ The German court asked the ECJ to decide whether the freedom of establishment provisions preclude a determination of a company's legal capacity under the laws of the seat state.¹⁸⁶ The court also asked whether the relevant Treaty provisions require a determination of a company's legal capacity based on the laws of the incorporation state.¹⁸⁷ In essence, the German Federal Court of Justice sought guidance on the ECJ's preference for the real seat doctrine or state-of-incorporation theory.¹⁸⁸ However, the ECJ's holdings do not directly correspond to

limitation on a company's right of establishment).

181. See *supra* note 180 and accompanying text (acknowledging the possibility of valid partial restrictions on the right of establishment); see also *Überseering*, 2002 E.C.R. ¶ 92-93 (conceding that strong public interest objectives might justify a host country's restriction of a foreign-incorporated company's freedom of establishment, but maintaining that such considerations do not justify a complete repudiation of the right).

182. See *Überseering*, 2002 E.C.R. ¶¶ 94-95 (holding that a host state's denial of the legal capacity of a foreign-incorporated entity is incompatible with the Treaty provisions on the freedom of establishment).

183. *Id.* ¶ 94.

184. *Id.* ¶ 95.

185. See *infra* notes 186-90 and accompanying text.

186. See *Überseering*, 2002 E.C.R. ¶ 21 (reciting the first question that the German Federal Court of Justice certified to the ECJ).

187. See *id.* (reciting the second question that the German Federal Court of Justice certified to the ECJ).

188. See Heine, *supra* note 48, at 103 (remarking that the *Centros* decision did not state whether the state-of-incorporation theory or the real seat theory should govern conflict-of-laws questions in the European Union and that the German Federal Court

the German court's questions. The ECJ did not directly express a preference for the real seat theory or the incorporation theory.¹⁸⁹ Instead, the ECJ simply stated that host states may not deny a foreign company legal capacity and that the freedom of establishment provisions, in fact, require host states to recognize the legal capacity of foreign entities.¹⁹⁰ While the ECJ has the liberty to rephrase a national court's question to make it compliant with its mandate, the Court's evasion of the choice between the real seat doctrine and incorporation theory was arguably intentional. The ECJ may have sought to pressure EU Member States to reach an agreement regarding the preferred doctrine.

The ECJ correctly concluded that the German requirement of reincorporation constituted an illegitimate restriction on the freedom of establishment.¹⁹¹ It would have been helpful, however, if the Court had expressed more clearly what type of overriding requirements of the public interest could sufficiently justify a restriction on the freedom of establishment.¹⁹² In the absence of clear guidance, legal uncertainty will continue to exist until the ECJ rules on a future case that tests the limits of the public interest exception.¹⁹³ The extent to which a host state can impose regulatory protections on a foreign corporation, short of completely negating the corporation's freedom of establishment, remains to be seen.¹⁹⁴

of Justice expected the ECJ to address in the *Überseering* case which of the two competing conflict-of-laws principles it preferred).

189. See *id.* ¶¶ 94-95 (holding that the Treaty provisions on freedom of establishment mandate the recognition of the legal capacity of a foreign-incorporated company but failing to state a preference for a conflict-of-laws theory).

190. *Id.*

191. See discussion *supra* Parts II.B.2 and II.B.3 (analyzing the ECJ's findings regarding whether a restriction on the freedom of establishment had occurred in the *Überseering* case and whether a justification existed for the restriction).

192. See *Überseering*, 2002 E.C.R. ¶ 92 (stating merely that imperative requirements of the public interest may "in certain circumstances and subject to certain conditions" constitute a justification for a restriction of the right of establishment); see also Dammann, *supra* note 48, at 651-52 (discussing the ECJ's failure to provide clear guidance regarding the public interest exception).

193. See Steinbeis, *supra* note 5 (noting that currently the uncertainty continues regarding the extent of the public interest exception and pointing out that the case law must define its boundaries); see also Brandner, *supra* note 68 (explaining that national law must fill the gaps of the *Überseering* ruling).

194. See *supra* note 193 and accompanying text (acknowledging the legal questions that remain unanswered following the *Überseering* ruling); Brandner, *supra* note 68 (suggesting that compelling public interest grounds may justify a restriction of the freedom of establishment).

III. IMPACT OF THE *ÜBERSEERING* CASE

The ECJ's decision in *Überseering* significantly alters German international company law as well as the company law of several other EU Member States.¹⁹⁵ While the ECJ's ruling in *Überseering* doubtlessly weakened the real seat doctrine,¹⁹⁶ two contrary interpretations are possible that would impute a different impact on the seat theory.¹⁹⁷ Under a broad interpretation of the Court's ruling, *Überseering* could be seen as abolishing the real seat doctrine and adopting the incorporation theory.¹⁹⁸ This Note argues, however, that the more reasonable interpretation is a narrow one that merely modifies the real seat doctrine to ensure legal recognition of foreign-incorporated companies.¹⁹⁹ While the *Überseering* decision demands that a host state recognize the legal capacity of a foreign corporation, it does not require that all other internal affairs of the company be regulated with reference to the laws of the incorporation state.²⁰⁰ In fact, the ECJ's ruling does not state anything about which countries' laws will apply after that initial recognition. The Court left open the question of whether the laws of the incorporation state or the seat state should exercise regulatory and enforcement control over such companies.²⁰¹

195. See Holst, *supra* note 48, at 323 (stating that various EU Member States that follow the real seat doctrine require companies to reincorporate under the host state's laws as a prerequisite to legal recognition if they move their central management there).

196. See DR. GÖTZ-SEBASTIAN HÖK, KANZLEI DR. HÖK, STIEGLMEIER & KOLLEGEN, ZUR RECHTSENTWICKLUNG NACH DER LIBERALISIERUNG DER AUSLANDSGRÜNDUNGEN DURCH DIE ÜBERSEERING-ENTSCHEIDUNG DES EUGH IN DEUTSCHLAND, at <http://www.dr-hoek.de/Auslandsgruendung-Ueberseering-Entscheidung-EuGH-Deutschland.html> (last updated May 2003) (on file with the American University Law Review) (arguing that a generalization of the ECJ's reasoning in *Überseering* leads to a significant curtailment of the application of the real seat doctrine).

197. See *infra* notes 198-99 and accompanying text (outlining broad and narrow interpretations of the ECJ's *Überseering* ruling).

198. See, e.g., Heine, *supra* note 48, at 103 (claiming that the ECJ adopted the incorporation theory in its *Überseering* decision); see also HÖK, *supra* note 196 (suggesting that the ECJ's *Überseering* ruling constitutes the beginning of the end of the real seat doctrine).

199. See, e.g., Mayr, *supra* note 152 (advocating that the ECJ did not intend to abolish the real seat doctrine and adopt the incorporation theory in its *Überseering* ruling).

200. See Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶ 95 (requiring merely that host states recognize the legal capacity of foreign-incorporated entities and grant them access to the national courts), available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002).

201. See Mayr, *supra* note 152 (theorizing that it remains unsettled whether the law of the seat state or the law of the state of incorporation should govern a corporation once the host state has recognized its legal capacity); see also Kersting, *supra* note 43, at 40 (arguing that the Court's holding that host states must recognize the legal capacity of foreign corporations does not automatically abolish the real seat doctrine); VANOVAC, *supra* note 105 (declaring that in neither *Centros* nor *Überseering*

Thus, the *Überseering* ruling could reasonably be interpreted as holding that the real seat doctrine is compatible with the treaty provisions on freedom of establishment as long as its application does not lead to the denial of a company's legal capacity.

Regardless of the debate over the continued existence of the real seat doctrine, the *Überseering* ruling allows promoters a greater choice of law and paves the way to the mutual recognition of companies among EU Member States.²⁰² The ECJ has required that host states recognize the legal capacity of companies that have their place of management in that state but are incorporated elsewhere and grant those companies access to the local courts.²⁰³ This means that companies may incorporate in one EU Member State while intending to conduct their business exclusively in another Member State that must now recognize the entity's legal capacity.²⁰⁴ This development

did the ECJ determine if and to what extent the law of the incorporation state or seat state applies to the legal circumstances of a company, such as creditor protection). This interpretation also corresponds to the Opinion of the Advocate General, who advised the Court to focus on the denial of legal capacity and access to courts that *Überseering BV* faced under German law. See Opinion of the Advocate General Colomer, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919 (on file with the American University Law Review). Implied in this statement is the suggestion to refrain from making a general ruling on the legitimacy of the real seat doctrine as a conflict-of-laws principle. Instead, the Court was to limit its analysis to the legality of a host state's non-recognition of a foreign company, which had ultimately resulted from the application of the real seat doctrine in the particular case. *Id.*

202. See, e.g., Heine, *supra* note 48, at 102 (predicting that the *Überseering* decision will result in the "mutual recognition of national business forms" within the European Union); see also Roger Frick, *Consolidating the Developments in Liechtenstein as Member State of EEA (European Economic Area)—Allgemeines Treuunternehmen (Allgemeines Treuunternehmen, Liechtenstein)*, Apr. 25, 2003, at 3 (on file with the American University Law Review) (concluding that the ECJ's attitude reflects a firm backing of the free movement of capital and persons within the European Union, which encourages EU Member States to recognize one another's business entities). The ECJ's ruling in *Überseering* does not apply to companies incorporated outside of the European Union that have a seat in an EU Member State, because the Treaty provisions on freedom of establishment only benefit companies incorporated and based within the European Union. See Herrmann, *supra* note 65, at 44; cf. Peter C. Fischer & Brian T. Hemphill, *Citizens of the World? New German Rules on Corporate Citizenship for U.S. Corporations*, 32 A.B.A. SEC. INT'L LAW & PRACTICE 22 (2003) (discussing a recent ruling by the German Federal Court of Justice that requires German courts to recognize the legal capacity of a company that was incorporated in the United States but has its main seat in Germany).

203. See *Überseering*, 2002 E.C.R. ¶ 95 (declaring that the Treaty provisions on freedom of establishment require the recognition of a company's legal capacity by the host state).

204. See HÖK, *supra* note 196 (setting forth that the establishment of pseudo-foreign corporations is legitimate after the *Überseering* ruling); see also Steinbeis, *supra* note 5 (arguing that the ECJ's *Überseering* ruling will make it easier for promoters to circumvent the costs of establishing a limited liability company in Germany because German courts will now have to recognize such cheap limited liability companies ("Billig-GmbHs") that have been formed according to less stringent regulations in other EU Member States). See generally Kersting, *supra* note 43, at 1 (explaining that

raises the possibility of a race to the bottom, where promoters seek to incorporate in the EU Member State with the least stringent corporate laws while intending to conduct their business elsewhere.²⁰⁵ In turn, this may lead to “regulatory competition” among EU Member States regarding their respective company laws.²⁰⁶

Due to this potential trend towards a race to the bottom, the ECJ’s *Überseering* ruling may, in fact, produce a greater incentive for Member States to work towards legal harmonization in the area of company law by agreeing to a set of minimum standards.²⁰⁷ While the EU Member States have pursued legal harmonization in some areas, neither primary nor secondary EU law contains harmonized legislation on corporations.²⁰⁸ In fact, significant discrepancies persist between the company laws of different Member States.²⁰⁹ For

pseudo-foreign corporations do not have a significant relationship with their state of incorporation). Pseudo-foreign corporations make it more difficult to ascertain the applicable law and to protect shareholders, and they generally interfere with a state’s interest in regulating companies. *Id.*

205. See, e.g., Heine, *supra* note 48, at 103 (anticipating regulatory competition between the corporate laws of EU Member States as a result of the *Überseering* ruling because companies will want to incorporate under the most suitable company law standards); cf. Kersting, *supra* note 43, at 39 (suggesting that the real seat doctrine counteracts the attempt by pseudo-foreign corporations to circumvent the corporate laws of the country where they carry on the majority of their business).

206. See Heine, *supra* note 48, at 102 (explaining that regulatory competition between Member States with respect to company laws may increase as a result of the *Überseering* decision). While proponents of regulatory competition predict a welfare-enhancing race to the top of legal standards (“California Effect”), opponents fear a race to the bottom similar to the “Delaware Effect” in the United States. *Id.* at 104-05. Viewing law as a product, the former school of thought believes that regulatory competition would increase the quality and efficiency of corporate laws. *Id.* at 104. By contrast, opponents of regulatory competition believe that certain market failures would prevent a race to the top and instead reduce the quality of corporate laws. *Id.* at 104-05. The rationale is that companies would seek the corporate regulations with the best cost-quality ratio, which would eventually lead jurisdictions to offer corporate laws with ever-lower prices without the incentive to increase the quality of the rules. *Id.* In Europe, the prevalent view seems to be that regulatory competition has detrimental effects, while most American scholars believe that it works to the advantage of shareholders. Kersting, *supra* note 43, at 11-12. In general, those who believe that regulatory competition leads to a race to the top will favor the incorporation theory, while those who believe that it leads to a race to the bottom will support the real seat doctrine. Heine, *supra* note 48, at 106.

207. See discussion *infra* Part IV.D.

208. See Holst, *supra* note 48, at 338 (describing the European Union’s history of failed attempts at legal harmonization of company laws, including the Convention on the Mutual Recognition of Companies and Convention on Insolvency Proceedings, which both the Netherlands and United Kingdom declined to ratify); see also ARNULL, *supra* note 66, at 469 (noting that Article 44(2)(g) of the EC Treaty is intended to promote harmonization and has been the basis for the adoption of some directives). See generally Christoph U. Schmid, *Pattern of Legislative and Adjudicative Integration of Private Law*, 8 COLUM. J. EUR. L. 415, 417-83 (2002) (surveying legislative and adjudicative integration in the European Union).

209. See Garza, *supra* note 48, at 77 (arguing that the variation among EU Member States’ company laws creates confusion and uncertainty for corporations); see also

example, Germany's rules on the establishment of corporations are substantially more restrictive than the laws in other Member States, such as the United Kingdom.²¹⁰ Harmonized legislation regarding corporate rules would weaken a company's incentive to circumvent national rules by incorporating elsewhere and, thus, diminish the roles of the real seat doctrine and incorporation theory as competing approaches to conflict-of-laws problems.

IV. RECOMMENDATIONS

A. *EU Member States Should Amend Their Laws to Comply with the ECJ Ruling*

To comply with the ECJ ruling in *Überseering*, EU Member States must review their international company laws and, if necessary, amend them to ensure legal recognition and access to courts for companies that have their seat in one Member State but are incorporated in another.²¹¹ In particular, Germany must eliminate its requirement of reincorporation that it imposed on foreign companies who moved their place of management to Germany and sought to bring legal proceedings there.²¹² Germany may seek to replace this reincorporation requirement with other methods of regulatory enforcement. While the German Federal Court of Justice has already implemented the ECJ's ruling in follow-up proceedings to the *Überseering* case,²¹³ German law is not well-prepared for the implications of the liberalization of foreign incorporation that will

Steinbeis, *supra* note 5 (stating that German company law is stricter than that of other EU Member States).

210. See Steinbeis, *supra* note 5 (illustrating the dissimilarities of company law within the European Union by comparing the regulations on the incorporation of companies in Germany and England). Promoters may form a limited liability company in England with a minimum capital of only £ 100, whereas they would need at least € 25,000 in Germany. *Id.* The higher minimum capital requirement in Germany is intended to guarantee greater creditor protection in exchange for liberating the company members from personal liability. *Id.*

211. See Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶ 95 (requiring host states to recognize the legal capacity of companies that are incorporated in another EU Member State but move their seat to the host state and grant those entities access to the host state's national courts), available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002).

212. See *id.* ¶¶ 81-82 (rejecting the German requirement of reincorporation as inconsistent with the freedom of establishment under the EC Treaty).

213. See Judgment of March 13, 2003, Bundesgerichtshof (German Federal Court of Justice) VII ZR 370/98, BGH ZIP 2003, 718; see also HÖK, *supra* note 196 (relating that the German Federal Court of Justice has given effect to the ECJ ruling in *Überseering* by declaring that the legal capacity of foreign entities must be recognized in Germany even if these companies have moved their place of administration to Germany).

occur in the aftermath of the *Überseering* ruling.²¹⁴ German lawmakers must attempt to resolve open questions such as the personal liability of the company members and partners of a foreign-incorporated entity with its seat in Germany and the integration of such a company into a German limited partnership.²¹⁵

B. *The ECJ Ruling in Überseering Should Be Interpreted Narrowly*

The holdings of the ECJ in the *Überseering* case cannot be construed as abolishing the real seat doctrine.²¹⁶ Instead, the *Überseering* decision should be interpreted narrowly as modifying, but not abolishing, the real seat doctrine.²¹⁷ Under a narrow interpretation, the *Überseering* ruling imposes on the host state the requirement of legal recognition of foreign-incorporated companies that have moved their centers of administration to that state.²¹⁸ The ECJ only rejected Germany's strict requirement of reincorporation.²¹⁹ The ECJ did not, however, discuss which states' law would apply to the internal structure of companies incorporated in one EU Member State and having their place of management in another.²²⁰ A narrow interpretation of the *Überseering* ruling is imperative to prevent the race to the bottom that would result from companies' ability to circumvent the legal, economic, and social values of host states.²²¹

214. See HÖK, *supra* note 196 (proclaiming that the German legal system is not prepared for the implications of foreign incorporations).

215. See *id.* (detailing some of the open questions in German international company law after the *Überseering* decision). German lawmakers also need to resolve issues concerning the ability of foreign-incorporated entities with a seat in Germany to be recorded in the land registry and register of companies. *Id.*

216. See discussion *supra* Part III (presenting two contrary interpretations of the *Überseering* case and the respective impacts on the real seat doctrine); Kersting, *supra* note 43, at 40 (arguing that the *Überseering* decision does not abolish the real seat doctrine).

217. See discussion *supra* Part III (arguing that the more reasonable interpretation is that *Überseering* merely modifies the seat theory to ensure legal recognition of companies incorporated in other EU Member States).

218. See discussion *supra* Part III (explaining that under a narrow interpretation, the ECJ's ruling demands a host state's recognition of the legal capacity of a foreign corporation but does not require other internal affairs of the company to be regulated by the laws of the incorporation state).

219. Case C-208/00, *Überseering BV v. Nordic Constr. Co. Baumanagement GmbH*, 2002 E.C.R. I-9919, ¶ 95, available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexplus!prod!CELEXnumdoc&lg=en&numdoc=62000J0208 (Nov. 5, 2002).

220. See *supra* note 201 and accompanying text (showing that the ECJ limited its analysis to the legality of non-recognition of a foreign company and refrained from ruling generally on the applicability of the seat theory in conflict-of-laws situations).

221. See discussion *supra* Part III (arguing that a broader interpretation would allow companies to incorporate in EU Member States with less stringent laws while intending to conduct their business exclusively in another state in an effort to avoid more restrictive laws); see also *supra* notes 205-06 (explaining the concept of a race to

C. Even Under a Broad Interpretation, Host States May Require Compliance with Their Regulatory Protections

If legal scholars largely interpret the *Überseering* ruling broadly, host states should be allowed to require companies doing business in their territory to follow basic standards of the host state's company law. This would prevent companies from circumventing those regulations by incorporating in a country with less stringent rules.²²² The ECJ's decision leaves room for host states to impose their regulatory protections on those companies that have their principal place of business in the host state but are incorporated in another EU Member State.²²³ The ECJ stated that compelling considerations of the public interest may justify a restriction on the freedom of establishment.²²⁴ The protection of creditors, minority shareholders, and employees in Germany may qualify as such public interest considerations.²²⁵ National courts and the ECJ will have to determine what the limitations are of a host state's ability to impose its regulatory framework.²²⁶ Presumably, the limit will be set where the

the bottom).

222. See Garza, *supra* note 48, at 82 (suggesting that a host state may be able to apply its company laws to those entities that have "substantial contacts" with that country, even if their place of incorporation is another EU Member State); Ebke, *supra* note 27, at 1016, 1029 (relating that some countries that adhere to the incorporation theory impose limitations on the application of the doctrine by requiring foreign-incorporated entities to follow the internal affairs rules of the state where they conduct most of their business).

223. See Steinbeis, *supra* note 5 (citing a legal scholar from Germany's Bucerius Law School as saying that the ECJ left a door open for the welfare desire of German company law by conceding that overriding considerations of the public interest may justify a restriction on the freedom of establishment).

224. See *Überseering*, 2002 E.C.R. ¶¶ 92-93 (giving examples of important public interest considerations that might justify a limited restriction on the freedom of establishment). These justifications include the protection of creditor and minority shareholder interests as well as the interests of employees and taxation authorities. *Id.* ¶ 92. The Court cautioned, however, that these interests will excuse restrictions on the right of establishment only "in certain circumstances and subject to certain conditions." *Id.* Even with the goal of protecting these interests, the restrictive measures may never go so far as to deny a company's legal capacity, because that would negate the right of establishment in its entirety. *Id.* ¶ 93.

225. See Steinbeis, *supra* note 5 (inferring from the ECJ's reasoning that German company law provisions that seek to protect creditors, minority shareholders, and employees may justify a restricted right of establishment); see also Dammann, *supra* note 48, at 685 (arguing that Germany could legitimately apply its rules on workers' participation in management to pseudo-foreign corporations). While the German provisions on codetermination constitute a restriction on the freedom of establishment, overriding requirements of the general interest would largely justify that restriction. *Id.* at 685.

226. See Steinbeis, *supra* note 5 (relating that German case law will have to fill in the gaps of where the limits are of Germany's ability to impose its regulatory protections short of negating the freedom of establishment). Currently, legal uncertainty exists in this area. *Id.*

imposition of these national regulations comes too close to an outright negation of the freedom of establishment.²²⁷

D. The European Union Should Strive Towards Legal Harmonization to Diminish Conflict-of-Laws Problems

More than anything, the ECJ ruling in *Überseering* increases the pressure on EU Member States to harmonize legislation in the area of company law.²²⁸ The potential for a race to the bottom in the aftermath of the *Überseering* decision may produce sufficient incentive for EU Member States to strive towards legal harmonization.²²⁹ Member states should agree to a set of minimum standards that companies must follow when doing business in any EU Member State and establish those in EU law.²³⁰ This harmonization would diminish the roles of the real seat doctrine and incorporation theory as alternative approaches to conflict-of-laws problems, because the law of the seat country and the law of the state of incorporation would be largely equivalent.²³¹

227. See *Überseering*, 2002 E.C.R. ¶¶ 93-94 (finding that national measures which amount to a negation of the right of establishment are incompatible with the Treaty provisions on the freedom of establishment). Of course, legitimate national measures would also have to meet the four-prong-test for the public interest exception. See DAVIES, *supra* note 83, at 148 (“[T]he rules must be applied in a non-discriminatory manner; they must be justified by imperative requirements in the general interest; they must be suitable for securing the attainment of the objective which they pursue; [and] they must not go beyond what is necessary to attain it.”); Dammann, *supra* note 48, at 647-85 (outlining the imperative requirements doctrine and analyzing its use for justifying national rules on codetermination).

228. See Garza, *supra* note 48, at 82 (observing that a blow to the seat theory could revive the strive towards legal harmonization in EU company law) (citing John C. Coffee, Jr., *European Takeovers: The 13th Directive is Coming*, 222 N.Y.L.J. 98 (Nov. 18, 1999)).

229. See Heine, *supra* note 48, at 103 (anticipating regulatory competition between the corporate laws of the EU Member States); Holst, *supra* note 48, at 332, 338-40 (proposing that legal harmonization would solve the race to the bottom problem).

230. See *supra* note 208 and accompanying text (discussing the lack of legal harmonization in the European Union in the area of company law); see also Garza, *supra* note 48, at 77 (advocating the adoption of “uniform rules of corporate governance” in order to ensure stability and progress in the economic sphere). See generally Schmid, *supra* note 208, at 416-17 (explaining that legal harmonization is achieved through directives, regulations, and ECJ rulings); Holst, *supra* note 48, at 338-39 (outlining the advantages and disadvantages of harmonizing legislation in the area of company law). For example, legal harmonization prevents the circumvention of national rules, but it may result in “high transaction costs.” *Id.* (citing David Charny, *Competition Among Jurisdictions in Formulating Corporate Law Rules: An American Perspective on the “Race to the Bottom” in the European Communities*, 32 HARV. INT’L L.J. 423, 436, 440 (1991)).

231. See Ebke, *supra* note 27, at 1037 (arguing that without harmonization of laws governing the internal affairs of EU corporations, competition for incorporation of businesses between EU Member States will be distorted); Schmid, *supra* note 208, at 485 (arguing that the adoption of a “European Civil Code” akin to the United States Uniform Commercial Code would serve to integrate the divergent national laws that

Until the achievement of legal harmonization in the area of company law, the European Union should devise strategies to control abuses of the freedom of establishment provisions to circumvent national regulations for the formation of a company.²³² Moreover, Member States should enter conventions about the mutual recognition of business forms and negotiate an approach to conflict-of-laws problems.²³³ Another way of diminishing the roles of competing conflict-of-laws principles would be the establishment of an EU corporation, the *Societas Europaea* (“SE”), which would be a business form that promoters could incorporate on an EU level and operate throughout the European Union.²³⁴

CONCLUSION

The ECJ limited its ruling in the *Überseering* case to the requirement that host states recognize a foreign-incorporated entity’s legal capacity and grant it access to the local courts. Accordingly, the decision should be interpreted narrowly as modifying the real seat doctrine to ensure legal recognition by host states. Because the ECJ did not determine which states’ laws should apply beyond this initial recognition, the holding cannot be interpreted broadly as abolishing the seat theory and adopting the incorporation doctrine. For now, the real seat doctrine continues to exist and must be deemed compatible with the freedom of establishment as long as it does not result in the denial of a foreign company’s legal capacity and access to the host state’s courts.

currently provide incentives for companies to abuse the freedom of establishment provisions).

232. See HÖK, *supra* note 196 (indicating that a legal basis for abuse control does not currently exist); M.CHETCUTI CAUCHI, CHETCUTI CAUCHI ADVOCATES, THE EUROPEAN COMPANY STATUTE: FREEDOM OF MOVEMENT OF THE SOCIETAS EUROPAEA (May 2001), available at www.cc-advocates.com/publications/articles/freedom-of-movement-european-company.htm (suggesting that some courts have ignored the corporate form and pierced the corporate veil to protect against abuse).

233. See ARNULL, *supra* note 66, at 469 (noting that the purpose of the Convention on the Mutual Recognition of Companies and Legal Persons is to reconcile the differences between the Member States’ rules regarding the recognition of foreign-incorporated entities). The European Union has not adopted this convention. *Id.*

234. See MEDHURST, *supra* note 83, at 185-86 (examining the possibility of the formation of a European company that would have a minimum capital requirement of €100,000 and would “operate on a homogenous European basis”); Heine, *supra* note 48, at 108 (noting that the SE is an attempt by the European Union to deter regulatory competition and preserve individual state models of corporate governance).